

## Rulemaking File

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**State of California  
Office of Administrative Law**

**In re:**  
**Board of Equalization**

**NOTICE OF APPROVAL OF REGULATORY  
ACTION**

**Regulatory Action:**

**Government Code Section 11349.3**

**Title 18, California Code of Regulations**

**OAL File No. 2013-0617-02 S**


**Amend sections: 4601, 4603, 4604, 4605**

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This regulatory action provides that all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) be served personally or by mail in the manner prescribed pursuant to Business and Professions Code section 22971.5. This action also amends three sections, one for retailers, one for wholesalers and distributors, and one for manufacturers and importers, to provide the Board with discretion to reduce a person's suspension for a violation of the Act to 5 days (currently the Board is limited to either 0, 10 or 20 days), when mitigating factors are present. This action also corrects cross-references within these amended sections.

OAL approves this regulatory action pursuant to section 11349.3 of the Government Code. This regulatory action becomes effective on 10/1/2013.

**Date: 7/16/2013**

  
\_\_\_\_\_  
George C. Shaw  
Senior Counsel

**For: DEBRA M. CORNEZ**  
Director

**Original: Cynthia Bridges**  
**Copy: Richard Bennion**

**RECEIVED**

**JUL 18 2013**

**Board Proceedings**

**OFFICE OF ADMINISTRATIVE LAW**

300 Capitol Mall, Suite 1250  
Sacramento, CA 95814  
(916) 323-6225 FAX (916) 323-6826



**DEBRA M. CORNEZ**  
Director

**MEMORANDUM**

TO: Richard Bennion  
FROM: OAL Front Desk  
DATE: 7/17/2013  
RE: Return of Approved Rulemaking Materials  
OAL File No. 2013-0617-02S

OAL hereby returns this file your agency submitted for our review (OAL File No. 2013-0617-02S regarding Service of a Notice of Violation or Warning Notice).

If this is an approved file, it contains a copy of the regulation(s) stamped "ENDORSED APPROVED" by the Office of Administrative Law and "ENDORSED FILED" by the Secretary of State. The effective date of an approved regulation is specified on the Form 400 (see item B.5). **Beginning January 1, 2013**, unless an exemption applies, Government Code section 11343.4 states the effective date of an approved regulation is determined by the date the regulation is filed with the Secretary of State (see the date the Form 400 was stamped "ENDORSED FILED" by the Secretary of State) as follows:

- (1) **January 1** if the regulation or order of repeal is filed on September 1 to November 30, inclusive.
- (2) **April 1** if the regulation or order of repeal is filed on December 1 to February 29, inclusive.
- (3) **July 1** if the regulation or order of repeal is filed on March 1 to May 31, inclusive.
- (4) **October 1** if the regulation or order of repeal is filed on June 1 to August 31, inclusive.

If an exemption applies concerning the effective date of the regulation approved in this file, then it will be specified on the Form 400. The Notice of Approval that OAL sends to the state agency will contain the effective date of the regulation. The history note that will appear at the end of the regulation section in the California Code of Regulations will also include the regulation's effective date. Additionally, the effective date of the regulation will be noted on OAL's Web site once OAL posts the Internet Web site link to the full text of the regulation that is received from the state agency. (Gov. Code, secs. 11343 and 11344.)

**Please note this new requirement:** Government Code section 11343 now requires:

1. Section 11343(c)(1): Within 15 days of OAL filing a state agency's regulation with the Secretary of State, the state agency is required to post the regulation on its Internet Web site in an easily marked and identifiable location. The state agency shall keep the regulation posted on its Internet Web site for at least six months from the date the regulation is filed with the Secretary of State.
2. Section 11343(c)(2): Within five (5) days of posting its regulation on its Internet Web site, the state agency shall send to OAL the Internet Web site link of each regulation that the agency posts on its Internet Web site pursuant to section 11343(c)(1).

OAL has established an email address for state agencies to send the Internet Web site link to for each regulation the agency posts. Please send the Internet Web site link for each regulation posted to OAL at **postedregslink@oal.ca.gov**.

**DO NOT DISCARD OR DESTROY THIS FILE**

Due to its legal significance, you are required by law to preserve this rulemaking record. Government Code section 11347.3(d) requires that this record be available to the public and to the courts for possible later review. Government Code section 11347.3(e) further provides that “....no item contained in the file shall be removed, altered, or destroyed or otherwise disposed of.” See also the Records Management Act (Government Code section 14740 et seq.) and the State Administrative Manual (SAM) section 1600 et seq.) regarding retention of your records.

If you decide not to keep the rulemaking records at your agency/office or at the State Records Center, you may transmit it to the State Archives with instructions that the Secretary of State shall not remove, alter, or destroy or otherwise dispose of any item contained in the file. See Government Code section 11347.3(f).

Enclosures

## NOTICE PUBLICATION/REGULATION SUBMISSION

**REGULAR**

(See instructions on reverse)

For use by Secretary of State only

STD. 400 (REV. 01-2013)

OAL FILE NUMBERS	NOTICE FILE NUMBER	REGULATORY ACTION NUMBER	EMERGENCY NUMBER
Z-		2013-0617-025	

For use by Office of Administrative Law (OAL) only

2013 JUN 17 P 1:56

OFFICE OF  
ADMINISTRATIVE LAW

NOTICE

REGULATIONS

AGENCY WITH RULEMAKING AUTHORITY  
State Board of Equalization

AGENCY FILE NUMBER (If any)

**A. PUBLICATION OF NOTICE (Complete for publication in Notice Register)**

1. SUBJECT OF NOTICE		TITLE(S)	FIRST SECTION AFFECTED	2. REQUESTED PUBLICATION DATE
3. NOTICE TYPE <input type="checkbox"/> Notice re Proposed Regulatory Action <input type="checkbox"/> Other		4. AGENCY CONTACT PERSON	TELEPHONE NUMBER	FAX NUMBER (Optional)
OAL USE ONLY	ACTION ON PROPOSED NOTICE <input type="checkbox"/> Approved as Submitted <input type="checkbox"/> Approved as Modified <input type="checkbox"/> Disapproved/Withdrawn		NOTICE REGISTER NUMBER	PUBLICATION DATE

**B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)**

1a. SUBJECT OF REGULATION(S) Service of a Notice of Violation or Warning Notice		1b. ALL PREVIOUS RELATED OAL REGULATORY ACTION NUMBER(S)	
2. SPECIFY CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)			
SECTION(S) AFFECTED (List all section number(s) individually. Attach additional sheet if needed.)		ADOPT	
TITLE(S) 18		AMEND 4601, 4603, 4604, 4605	
		REPEAL	
3. TYPE OF FILING			
<input checked="" type="checkbox"/> Regular Rulemaking (Gov. Code §11346) <input type="checkbox"/> Resubmittal of disapproved or withdrawn nonemergency filing (Gov. Code §11349.3, 11349.4) <input type="checkbox"/> Emergency (Gov. Code, §11346.1(b)) <input type="checkbox"/> Certificate of Compliance: The agency officer named below certifies that this agency complied with the provisions of Gov. Code §11346.2-11347.3 either before the emergency regulation was adopted or within the time period required by statute. <input type="checkbox"/> Resubmittal of disapproved or withdrawn emergency filing (Gov. Code, §11346.1) <input type="checkbox"/> Emergency Readopt (Gov. Code, §11346.1(h)) <input type="checkbox"/> File & Print <input type="checkbox"/> Other (Specify) _____ <input type="checkbox"/> Changes Without Regulatory Effect (Cal. Code Regs., title 1, §100) <input type="checkbox"/> Print Only			
4. ALL BEGINNING AND ENDING DATES OF AVAILABILITY OF MODIFIED REGULATIONS AND/OR MATERIAL ADDED TO THE RULEMAKING FILE (Cal. Code Regs. title 1, §44 and Gov. Code §11347.1)			
5. EFFECTIVE DATE OF CHANGES (Gov. Code, §§ 11343.4, 11346.1(d); Cal. Code Regs., title 1, §100)			
<input checked="" type="checkbox"/> Effective January 1, April 1, July 1, or October 1 (Gov. Code §11343.4(a)) <input type="checkbox"/> Effective on filing with Secretary of State <input type="checkbox"/> \$100 Changes Without Regulatory Effect <input type="checkbox"/> Effective other (Specify) _____			
6. CHECK IF THESE REGULATIONS REQUIRE NOTICE TO, OR REVIEW, CONSULTATION, APPROVAL OR CONCURRENCE BY, ANOTHER AGENCY OR ENTITY			
<input type="checkbox"/> Department of Finance (Form STD. 399) (SAM §6660) <input type="checkbox"/> Fair Political Practices Commission <input type="checkbox"/> State Fire Marshal <input type="checkbox"/> Other (Specify) _____			
7. CONTACT PERSON Richard E. Bennion		TELEPHONE NUMBER (916) 445-2130	FAX NUMBER (Optional) (916) 324-3984
		E-MAIL ADDRESS (Optional) rbennion@boe.ca.gov	

8. I certify that the attached copy of the regulation(s) is a true and correct copy of the regulation(s) identified on this form, that the information specified on this form is true and correct, and that I am the head of the agency taking this action, or a designee of the head of the agency, and am authorized to make this certification.

SIGNATURE OF AGENCY HEAD OR DESIGNEE

DATE

June 17, 2013

TYPED NAME AND TITLE OF SIGNATORY

Joann Richmond, Chief, Board Proceedings Division

For use by Office of Administrative Law (OAL) only

ENDORSED APPROVED

JUL 16 2013

Office of Administrative Law

**Final Text of Proposed Amendments to  
California Code of Regulations, Title 18, Sections  
4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*,  
4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and  
4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

**4601. Service of a Notice of Violation or Warning Notice.**

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5. ~~The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub-post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.~~

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22971.5~~22974.7, 22978.7 and 22979.7~~, Business and Professions Code.

**4603. Penalties for Licensed or Unlicensed Retailers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).
- (2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3, subdivision (a)(2) or subdivision (a)(4), 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22973(a)(5), 22974, 22974.3, 22974.4, 22974.7, 22980.1(c), (d), (e) and (g), 22980(b), 22980.2(a) and 22980.3(a)(2) and (d), Business and Professions Code.

#### **4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).
- (2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).
- (3) Business and Professions Code section 22978.5<sub>2</sub> subdivision (b) (distributor's or wholesaler's failure to retain sales records).
- (4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

- (1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).
- (2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).



(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4~~22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, 22977(a)(5), 22978.1, 22978.2, ~~22978.7~~, 22978.5(b), 22978.7, 22979.7, 22980(b), 22980.1(b), (c), (d), (e), (f) and (g), ~~and 22980.2(a) and 22980.3(a)(2) and (d)~~, Business and Professions Code.

#### **4605. Penalties for Licensed or Unlicensed Manufacturers and Importers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).
- (2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).
- (3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).
- (4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).
- (6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

(b) A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)) shall result in a 20-day suspension.

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

(d) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, ~~22978.7~~, ~~22979.4~~, 22979(b)(1), ~~22979.4~~, 22979.5(b), ~~22979.6(c)~~, 22979.7, 22980.1(a), (e) and (f), 22980.2(a), and ~~22980.3(a)(2) and (d)~~ ~~22979.6(e)~~, Business and Professions Code.

publication titled *Accreditation Standards and Procedures* (LAAB Standards). The LAAB Standards are used nationally for accrediting college and university degree programs in landscape architecture. The proposed amendments are intended to update Section 2620.5 to conform to updates made to the LAAB Standards published by the Landscape Architectural Accreditation Board on February 6, 2010 (2010 LAAB Standards).

#### DECISION

On May 31, 2013, the Board submitted the above-referenced regulatory action to the Office of Administrative Law (OAL) for review in accordance with the Administrative Procedure Act (APA). On July 15, 2013, the OAL notified the Board of the disapproval of this regulatory action for failure to comply with the necessity standard of Government Code section 11349.1.

#### CONCLUSION

For the reason set forth above, OAL has disapproved this regulatory action. If you have any questions, please contact me at (916) 323-6809.

Date: July 17, 2013

Richard L. Smith  
Senior Counsel  
FOR: DEBRAM. CORNEZ  
Director

Original: Douglas McCauley  
Copy: John Keidel

### SUMMARY OF REGULATORY ACTIONS

#### REGULATIONS FILED WITH SECRETARY OF STATE

This Summary of Regulatory Actions lists regulations filed with the Secretary of State on the dates indicated. Copies of the regulations may be obtained by contacting the agency or from the Secretary of State, Archives, 1020 O Street, Sacramento, CA 95814, (916) 653-7715. Please have the agency name and the date filed (see below) when making a request.

File# 2013-0531-02  
BOARD OF BEHAVIORAL SCIENCES  
Marriage and Family Therapist Intern Experience

This regulatory action amends experience requirements for an applicant seeking licensure as a marriage and family therapist (LMFT) to make the experience requirements consistent with SB 363 (Stat. 2011, c. 384).

Title 16  
California Code of Regulations  
AMEND: 1833  
Filed 07/15/2013  
Effective 10/01/2013  
Agency Contact: Rosanne Helms (916) 574-7897

File# 2013-0617-02

#### BOARD OF EQUALIZATION

##### Service of a Notice of Violation or Warning Notice

This regulatory action provides that all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) be served personally or by mail in the manner prescribed pursuant to Business and Professions Code section 22971.5. This action also amends three sections, one for retailers, one for wholesalers and distributors, and one for manufacturers and importers, to provide the Board with discretion to reduce a person's suspension for a violation of the Act to 5 days (currently the Board is limited to either 0, 10 or 20 days), when mitigating factors are present. This action also corrects cross-references within these amended sections.

Title 18  
California Code of Regulations  
AMEND: 4601, 4603, 4604, 4605  
Filed 07/16/2013  
Effective 10/01/2013  
Agency Contact:  
Richard E. Bennion (916) 445-2130

File# 2013-0606-02

#### BOARD OF EQUALIZATION

##### Teleproduction or Other Postproduction Service Equipment

As part of the November 6, 2012, General Election, California voters approved Proposition 30, which added section 36 to article XIII of the California Constitution. Section 36, subdivision (f)(1), temporarily increases the state sales and use tax by one quarter of one percent for a four-year period from January 1, 2013 through December 31, 2016. Existing California Code of Regulations, title 18, sections 1532, 1533.1, 1533.2, 1534, 1535, and 1598 all describe partial exemptions from the tax provided by Revenue and Taxation Code sections 6356.5, 6356.6, 6357.1, 6357.7, 6358.5, or 6378, to which the temporary tax imposed by section 36 of article XIII of the California Constitution would apply. The State Board of Equalization amended sections 1532, 1533.1, 1533.2, 1534, 1535, and 1598 of title 18 of the California Code of Regulations as a change with-

## Rulemaking File Index

### Title 18. Public Revenue

Special Taxes Regulation 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*

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  - Minutes
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  - Deputy Director's Memo dated January 4, 2013
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  - Form 400 and Notice, Publication Date April 19, 2013
  - Proposed Text of Regulations 4601, 4603, 4604, and 4605
  - Email sent to Interested Parties, April 19, 2013
  - CA Regulatory Notice Register 2013, Volume No. 16-Z
10. [Notice to Interested Parties, April 19, 2013](#)

The following items are exhibited:

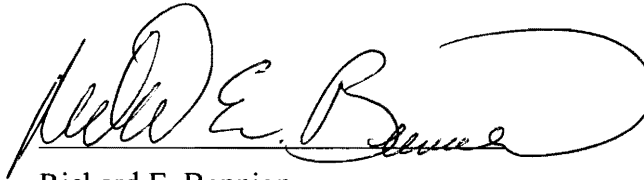
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  - Notice of Proposed Regulatory Action
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  - Proposed Text of Regulation 1566.1
  - Regulation History

## VERIFICATION

I, Richard E. Bennion, Regulations Coordinator of the State Board of Equalization, state that the rulemaking file of which the contents as listed in the index is complete, and that the record was closed on June 14, 2013 and that the attached copy is complete.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

June 14, 2013

A handwritten signature in black ink, appearing to read "Richard E. Bennion", written over a horizontal line.

Richard E. Bennion  
Regulations Coordinator  
State Board of Equalization

**Final Statement of Reasons for  
Adoption of Proposed Amendments to California Code of Regulations,  
Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*,  
4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and  
4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

Update of Information in the Initial Statement of Reasons

The factual basis, specific purpose, and necessity for, the problems to be addressed by, and the anticipated benefits from the proposed amendments to California Code of Regulations, title 18, sections (Regulations) 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*, are the same as provided in the initial statement of reasons. However, the Board, pursuant to Government Code section 11346.8, subdivision (c), added a comma after the reference to Business and Professions Code section “22974.3” in subdivision (f) of the text of the proposed amendments to Regulation 4603 and changed the period following the number “5” to a comma in subdivision (a)(3) of the text of the proposed amendments to Regulation 4604 to make the text of both regulations grammatically correct. The Board did not make any other changes to the text of the proposed amendments to Regulations 4601, 4603, 4604, and 4605.

The adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 was not mandated by federal law or regulations and there is no federal regulation that is identical to Regulation 4601, 4603, 4604, or 4605.

The Board did not rely on any data or any technical, theoretical, or empirical study, report, or similar document in proposing or adopting the amendments to Regulations 4601, 4603, 4604, and 4605 that was not identified in the initial statement of reasons, or which was otherwise not identified or made available for public review prior to the close of the public comment period.

In addition, the factual basis has not changed for the Board’s initial determination that the proposed regulatory action will not have a significant adverse economic impact on business and the Board’s economic impact analysis, which determined that the Board’s proposed regulatory action:

- Will neither create nor eliminate jobs in the State of California;
- Nor result in the elimination of existing businesses;
- Nor create or expand business in the State of California; and
- Will not affect the health and welfare of California residents, worker safety, or the state’s environment.

The proposed amendments may affect small business.

### No Mandate on Local Agencies or School Districts

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 does not impose a mandate on local agencies or school districts.

### Public Comments

The Board did not receive any written comments regarding the proposed regulatory action and no interested parties appeared at the June 11, 2013, public hearing to comment on the proposed regulatory action.

### Determinations Regarding Alternatives

By its motion, the Board determined that no alternative to the proposed amendments to Regulations 4601, 4603, 4604, and 4605 would be more effective in carrying out the purposes for which the amendments are proposed, would be as effective and less burdensome to affected private persons than the adopted amendments, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provisions of law.

Further, the Board did not reject any reasonable alternatives to the proposed amendments to Regulations 4601, 4603, 4604, and 4605 that would lessen any adverse impact the proposed amendments may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed amendments. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

Furthermore, the Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Cigarette and Tobacco Products Licensing Act (Act), which are included in the proposed amendments to Regulation 4601. The Board also anticipates that the Board and regulated persons will benefit from the proposed amendments to Regulations 4603 through 4605 because they establish a fair, 5-day suspension period to address such situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of 5 days would be more appropriate.

**Updated Informative Digest for**  
**Adoption of Proposed Amendments to California Code of Regulations,**  
**Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*,**  
**4603, *Penalties for Licensed or Unlicensed Retailers*,**  
**4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and**  
**4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

On June 11, 2013, the State Board of Equalization (Board) held a public hearing on and unanimously voted to adopt the proposed amendments to California Code of Regulations, title 18, sections (Regulations) 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*, described in the notice of proposed regulatory action. There have not been any changes to the applicable laws or the effect of the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 described in the informative digest included in the notice of proposed regulatory action. However, the Board, pursuant to Government Code section 11346.8, subdivision (c), added a comma after the reference to Business and Professions Code section “22974.3” in subdivision (f) of the text of the proposed amendments to Regulation 4603 and changed the period following the number “5” to a comma in subdivision (a)(3) of the text of the proposed amendments to Regulation 4604 to make the text of both regulations grammatically correct. The Board did not make any other changes to the text of the proposed amendments to Regulations 4601, 4603, 4604, and 4605.

The Board did not receive any written comments regarding the proposed regulatory action and no interested parties appeared at the public hearing on June 11, 2013, to comment on the proposed regulatory action. The informative digest included in the notice of proposed regulatory action provides:

“Current Law

“On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Act to the BPC. As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

“The Act is administered by the Board pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act’s licensing requirements. As relevant here, the Board adopted Regulation 4600,



*Issuance and Contents of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to a person that has been issued a citation for a violation of the Act, and the Board adopted Regulation 4601 to prescribe the manner in which a Notice of Violation or Warning Notice shall be served. The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

“The Board also adopted Regulations 4603, 4604, and 4605 to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

“Effect, Objectives, and Benefits of the Proposed Amendments to Regulations 4601, 4603, 4604, and 4605

*“Amendments to Regulation 4601*

“A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, the intent and objectives of the proposed amendments to Regulation 4601 are to make the regulation prescribe the manner of serving all of the notices the Board is required to serve under the Act, require that all of the notices be served in the manner prescribed for service of a notice under BPC section 22971.5, and generally ensure that the regulation is consistent with BPC section 22971.5. The Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

“The text of the proposed amendments to Regulation 4601 is slightly different than the text that the Board approved on June 26, 2012. The original text provided that “Any

notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law.” However, section 22971.5 was added to the BPC after the Board’s adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised the approved text of the amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board’s proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board’s proposed amendments provide that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5.”

#### *“Amendments to Regulations 4603 through 4605*

“Regulations 4603 through 4605 provide that a suspension period may be reduced to “0 days, 10 days, or 20 days” when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10 days would be appropriate. The intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to add a 5-day suspension period to the regulations to specifically give the Board additional flexibility to reduce suspensions based upon staff’s belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

“In addition, the intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to clarify the regulations’ cross-references to statutes that require the revocation of retailers’, wholesalers’, distributors’, manufacturers’, and importers’ licenses for specified violations of the Act; and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

“The proposed amendments also update the reference notes to Regulations 4601, 4603, 4604, and 4605 to better reflect the contents of each reference note’s regulation.

#### *“Business Taxes Committee Process*

“The Board approved the amendments to Regulation 4601, 4603, 4604, and 4605 (described above) during the Board’s June 26, 2012, Business Taxes Committee meeting, but, at the conclusion of the meeting, the Board voted to postpone proposing the amendments to Regulations 4601, 4603, 4604, and 4605 while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and

make specific other provisions of the Act. During the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 at this time, and the Board did not decide to propose to adopt a new regulation at that time.

"The Board has performed an evaluation of whether the proposed amendments to Regulations 4601, 4603, 4604, and 4605 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 4601 is the only state regulation prescribing the manner for serving a notice issued under the Act and Regulations 4603 through 4605 are the only state regulations prescribing the Board's discretion to reduce a suspension imposed under the Act. In addition, there are no comparable federal regulations or statutes to Regulations 4601, 4603, 4604, and 4605."



BOARD OF EQUALIZATION

**BUSINESS TAXES COMMITTEE MEETING MINUTES**

HONORABLE BETTY T. YEE, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

MEETING DATE: JUNE 26, 2012, TIME: 10:00 A.M.

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**ACTION ITEMS & STATUS REPORT ITEMS**

**Agenda Item No: 1**

**Title: Proposed Regulation 4801 and amendments to Regulations 4601, 4603, 4604, and 4605 under the Cigarette and Tobacco Products Licensing Act (Act).**

**Action 1**

**Proposed Amendments to Regulation 4601, *Service of a Notice of Violation or Warning.***

**Issue:**

Request approval and authorization to publish proposed amendments to Regulation 4601 to clarify the service requirements for notices issued under the Act.

**Committee Discussion:**

There was no discussion of this item.

**Committee Action:**

Upon motion by Mr. Horton and seconded by Mr. Runner, without objection, the Committee approved the proposed regulatory amendments.

There is no operative date, and implementation will take place 30 days after approval by the Office of Administrative Law. A copy of the proposed amendments to Regulation 4601 is attached.

**Action 2**

**Proposed Regulation 4801, *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person.***

**Issue:**

Request approval and authorization to publish proposed Regulation 4801 formalizing the current policy on transfers of cigarettes and tobacco products between retail stores owned by the same person.

**Committee Discussion:**

Staff introduced the topic for discussion. Mr. Steven Alari, representing SEIU Local 1000, stated his objection to staff's proposal and recommended that the Board adopt a regulation preventing the transfer of cigarettes and tobacco products. While some Board Members expressed support for the proposed regulation, there were also concerns raised that the regulation may not be clear in what constitutes "same legal entity." In addition, concerns were raised regarding adequate inventory controls when transferring products. Ms. Mandel also asked that staff include in the sample transfer log all the required elements to satisfy the inspectors.

**Committee Action:**

The Board directed staff to work with Investigation Division to further address these concerns, and bring the issue back to the Board in an expedited manner.

**Action 3**

***Proposed Amendments to Regulations 4603, Penalties for Licensed or Unlicensed Retailers; 4604, Penalties for Licensed or Unlicensed Wholesalers and Distributors, and 4605; Penalties for Licensed or Unlicensed Manufacturers and Importers.***

**Issue:**

Request approval and authorization to publish proposed amendments to Regulations 4603, 4604 and 4605, providing staff with additional flexibility in setting a period of suspension.

**Committee Discussion:**

Staff introduced the topic for discussion. Mr. Steven Alari, representing SEIU Local 1000, generally supported staff's recommendation and was opposed to the alternative that could have resulted in a suspension period less than 5 days. Ms. Steel expressed concern that a 5-day alternative would be imposed in lieu of a 0-day suspension. Staff noted that although in some cases this may be correct, in other cases what may have been a 10-day suspension may result in a 5-day suspension period. The Board Members raised concerns that the start date of the suspension period is always on a Friday and recommended that an alternative day be utilized, such as Monday to start the period of suspension.

**Committee Action:**

Upon motion by Mr. Runner, seconded by Mr. Horton, without objection, the Committee approved the proposed regulatory amendments, and directed staff to implement an alternative start day for suspension periods. A copy of the proposed amendments to Regulations 4603, 4604 and 4605 is attached.

/s/ Betty T. Yee

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Honorable Betty T. Yee, Committee Chair

/s/ Kristine Cazadd

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Kristine Cazadd, Executive Director

BOARD APPROVED

at the June 27, 2012 Board Meeting

/s/ Joann Richmond

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Joann Richmond, Chief  
Board Proceedings Division

**Regulation 4601. Service of a Notice of Violation or Warning Notice**

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law. The Notice of Suspension, Notice of Revocation, Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

**Regulation 4603. Penalties for Licensed or Unlicensed Retailers**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).

(2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision (b)).

(4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

**(b)** A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

**(d)** A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

**(e)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

**(f)** Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, ~~22978.6~~, or 22980.3, subdivision (a)(2) or subdivision (d).



**Regulation 4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).

(2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).

(3) Business and Professions Code section 22978.5, subdivision (b) (distributor's or wholesaler's failure to retain sales records).

(4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

**(b)** A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision. (b)).

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

**(d)** A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

**(e)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

**Regulation 4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors (Cont.)**

**(f)** Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

**Regulation 4605. Penalties for Licensed or Unlicensed Manufacturers and Importers**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).

(2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).

(3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).

(4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

**(b)** A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision. (b)) shall result in a 20-day suspension.

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

**(d)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

**(e)** Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4, 22978.6, or~~ 22980.3, subdivision (a)(2) or subdivision (d).



## STATE BOARD OF EQUALIZATION

PROPERTY AND SPECIAL TAXES DEPARTMENT  
50 N STREET, SACRAMENTO, CALIFORNIA  
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0063  
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BETTY T. YEE  
First District, San Francisco

SEN. GEORGE RUNNER (Ret.)  
Second District, Lancaster

MICHELLE STEEL  
Third District, Rolling Hills Estates

JEROME E. HORTON  
Fourth District, Los Angeles

JOHN CHIANG  
State Controller

KRISTINE CAZADD  
Executive Director

June 15, 2012

Dear Interested Party:

Enclosed are the Agenda, Issue Paper, and Revenue Estimate for the June 26, 2012, Business Taxes Committee meeting. This meeting will address proposed Regulation 4801, *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person* amendments to Regulation 4601, *Service of Notice of Violation or Warning Notice* and amendments to Regulations 4603, 4604, and 4605 involving penalties for licensed or unlicensed retailers, wholesalers, distributors, manufacturers and importers.

Action 1 on the Agenda concerns the agreed upon amendments to Regulation 4601 that expand the service requirements to include **any** notices required under the Cigarette and Tobacco Products Licensing Act (Act) and its Regulations.

Action 2 on the Agenda concerns proposed Regulation 4801 which formalizes the Board's current policy and documentation requirements on transfers of cigarettes and tobacco products between retail stores owned by the same person.

Action 3 on the Agenda concerns proposed amendments to Regulations 4603, 4604 and 4605 which provide Board staff additional flexibility in setting suspension periods for violations of the Act under appeal when mitigating circumstances are present.

Please feel free to publish this information on your website or otherwise distribute it to your associates, members, or other persons that may be interested in these issues. Thank you for the input on these issues and I look forward to seeing you at the Business Taxes Committee meeting at **10:00 a.m. on June 26, 2012**, in Room 121 at the address shown above.

Sincerely,

David J. Gau, Deputy Director  
Property and Special Taxes Department

DJG:pb

Enclosures

cc: (all with enclosures)

Honorable Jerome E. Horton, Chairman, Fourth District  
Honorable Michelle Steel, Vice Chair, Third District  
Honorable Betty T. Yee, Member, First District (MIC 71)  
Senator George Runner (Ret.), Member, Second District (MIC 78)  
Honorable John Chiang, State Controller, c/o Ms. Marcy Jo Mandel

(via email)

Ms. Regina Evans, Board Member's Office, Fourth District  
Mr. Robert Thomas, Board Member's Office, Fourth District  
Mr. Joel Angeles, Board Member's Office, Third District  
Mr. Neil Shah, Board Member's Office, Third District  
Mr. Tim Treichelt, Board Member's Office, Third District  
Mr. Alan LoFaso, Board Member's Office, First District  
Ms. Mengjun He, Board Member's Office, First District  
Ms. Yvette Stowers, Board Member's Office, First District  
Mr. Andrew Jacobson, Board Member's Office, First District  
Mr. James Kuhl, Board Member's Office, Second District  
Mr. Lee Williams, Board Member's Office, Second District  
Ms. Natasha Ralston Ratcliff, State Controller's Office  
Ms. Kristine Cazadd  
Mr. Randy Ferris  
Ms. Christine Bisauta  
Mr. Steven Smith  
Mr. Bradley Heller  
Ms. Lynn Bartolo  
Mr. Lou Feletto  
Mr. Randy Silva  
Ms. Debbie Kalfsbeek  
Ms. Kirsten Stark  
Ms. Leila Hellmuth  
Mr. Phillip Bishop  
Mr. Barry Ivy



**BOARD OF EQUALIZATION**

**BUSINESS TAXES COMMITTEE MEETING AGENDA**

HONORABLE BETTY YEE, COMMITTEE CHAIRWOMAN

450 N STREET, SACRAMENTO - ROOM 121

**JUNE 26, 2012 – 10:00 A.M.**

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1. Proposed Regulation 4801 and amendments to Regulations 4601, 4603, 4604, and 4605 under the Cigarette and Tobacco Products Licensing Act

Request authorization to publish Regulation 4801 regarding transfers of cigarettes and tobacco products between retail stores, and amendments to existing regulations regarding the serving of notices and periods of suspension

**AGENDA —June 26, 2012 Business Taxes Committee Meeting**  
***Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations 4601, 4603, 4604, and 4605***

<p><b>Action 1 — Agreed Upon Items: Proposed Amendments to Regulation 4601, Service of a Notice of Violation or Warning Notice.</b></p> <p>Agenda, page 3. Issue Paper Alternative 1, Item 2</p>	<p>Approve and authorize publication of amendments to Regulation 4601, as agreed upon by staff and interested parties.</p>
<p><b>Action 2 — Proposed Regulation 4801, Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person.</b></p> <p>Agenda, page 4 Issue Paper Alternative 1, Item 1</p> <p>Issue Paper Alternative 2, Item 1</p>	<p>Approve and authorize publication of either:</p> <p>Staff's proposed Regulation to provide for transfers of cigarettes and tobacco products between retail stores owned by the same legal entity that are supported by a transfer log or similar document and copies of invoices to be maintained at each location participating in the transfer.</p> <p style="text-align: center;">OR</p> <p>California Distributor's Association and SEIU Local 1000's proposal that any Regulation adopted should prohibit the transfer of cigarettes and tobacco products between any retail stores regardless of the ownership.</p>

**AGENDA — June 26, 2012 Business Taxes Committee Meeting**  
***Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations***  
***4601, 4603, 4604 and 4605***

<p><b>Action 3 — Proposed Amendments to Regulations 4603, Penalties for Licensed or Unlicensed Retailers, 4604, Penalties for Licensed or Unlicensed Wholesalers and Distributors, and 4605, Penalties for Licensed or Unlicensed Manufacturers and Importers.</b></p> <p>Agenda, page 6. Issue Paper Alternative 1 Item 3</p>	<p>Approve and authorize publication of either:</p> <p>Staff's proposed amendments to the Regulations, as recommended at the <b>second</b> interested parties meeting, providing staff with a 5 day suspension period in addition to the current, 0 day, 10 day and 20 day suspension periods that may be imposed when mitigating circumstances are present, including the recommended technical corrections.</p> <p>OR</p> <p>Staff's proposed amendments to the Regulations, as recommended at the <b>first</b> interested parties meeting, providing staff with a range of suspension periods between 0 days and 20 days that may be imposed when mitigating circumstances are present, including the recommended technical corrections. Although, staff is no longer recommending adoption of these amendments, the alternative language is being provided for the Board's consideration.</p>
<p>Issue Paper Alternative 2 Item 3</p>	



**AGENDA — June 26, 2012 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations**  
**4601, 4603, 4604 and 4605**

Action Item	Staff and Industry's Proposed Regulatory Language
<p><b>Action 1 — Agreed Upon Items</b> <b>Regulation 4601</b></p>	<p><b>Regulation 4601, Service of a Notice of Violation or Warning Notice</b>  Any notice issued under the Cigarette and Tobacco Products Licensing Act, may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code Section 30206 of the Cigarette and Tobacco Products Tax Law. <del>The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.</del></p>

**AGENDA — June 26, 2012 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations**  
**4601, 4603, 4604 and 4605**

Action Item	Regulatory Language Proposed by Staff	Recommendation by SEIU Local 1000 and California Distributor's Association
<b>Action 2 - Proposed Regulation 4801</b>	<p><u>Transfers of Cigarettes and Tobacco Products Between Retail Stores Owned by the Same Person.</u></p> <p><u>(a) GENERAL.</u> Every retailer of cigarettes and tobacco products is required to maintain purchase invoices for all cigarettes and tobacco products purchased and make those invoices available for inspection by the board or a law enforcement agency. A licensed retailer owning multiple locations who wishes to transfer cigarettes and tobacco products between its licensed locations shall prepare a transfer log or document at the time of transfer and maintain the records for four years from the date of transfer. A copy of the transfer log or document, accompanied by a copy of the original purchase invoice(s) documenting the purchase of each item transferred, must be kept at both the transferring and receiving locations involved in the transfer for at least one year after the transfer. Copies of original purchase invoices may be maintained at the receiving location on alternative storage media as prescribed in Regulation 4901 (h). The taxpayer must provide facilities and equipment for reading, locating, and reproducing any invoices maintained on alternative storage media.</p> <p><u>(b) SPECIFIC APPLICATION.</u> The transfer log or document shall show the following:</p> <p>(1) The transferring retail location, license information, supplier's name, invoice number, and the date the bulk cigarettes and</p>	<p>Do not adopt the proposed Regulation and consider prohibiting such transfers between retail stores regardless of ownership. Regulatory language was not provided by the interested parties nor prepared for consideration by staff.</p>

**AGENDA — June 26, 2012 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations**  
**4601, 4603, 4604 and 4605**

Action Item	Regulatory Language Proposed by Staff	Recommendation by SEIU Local 1000 and California Distributor's Association
Action 2 cont.	<p>tobacco products purchase was made;</p> <p>(2) <u>The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and,</u></p> <p>(3) <u>A legible itemized listing of cigarettes and tobacco products transferred including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.</u></p> <p>(c) <u>The transfer of cigarettes and tobacco products shall only be allowed when the legal entity licensed as the retailer for the retail location transferring the cigarettes and tobacco products is the same legal entity that is licensed as the retailer at the retail location receiving the cigarettes and tobacco products. As an example, a transfer between a location licensed as a sole proprietorship and a location licensed as a partnership where the sole proprietor is one of the partners would not qualify under this section since the same legal entity does not own both locations.</u></p> <p>(d) <u>Records of the transfer shall be made available to the board or its authorized representative for examination upon request. Failure to provide such documentation when requested can result in the seizure of the cigarettes or tobacco products that are claimed to be transferred and the issuance of a citation. Transfer logs or documents created or provided after a seizure and/or citation are not acceptable and cannot be used for the return of seized product or dismissal of a violation.</u></p>	

**AGENDA — June 26, 2012 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations**  
**4601, 4603, 4604 and 4605**

Action Item	Regulatory Language Proposed by Staff	Alternate Regulatory Language
<b>Action 3 - Regulation 4603 (f)</b>	<p>(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, <u>5 days</u>, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or 22974.4, <del>22978.6</del>, or 22980.3, subdivision (a)(2) or <u>subdivision (d)</u>.</p>	<p>(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be <u>within a range of 0 days, 10 days, or 20 days</u>. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, <del>22978.6</del>, or 22980.3, subdivision (a)(2) or <u>subdivision (d)</u>.</p>
<b>Regulation 4604 (f)</b>	<p>(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, <u>5 days</u>, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, <del>22978.2</del>, subdivision (a)(2) or <u>subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d)</u>.</p>	<p>(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be <u>within a range of 0 days, 10 days, or 20 days</u>. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, <del>22978.2</del>, subdivision (a)(2) or <u>subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d)</u>.</p>

**AGENDA — June 26, 2012 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations**  
**4601, 4603, 4604 and 4605**

Action Item	Regulatory Language Proposed by Staff	Alternate Regulatory Language
<p><b>Action 3 cont.</b> <b>Regulation</b> <b>4605 (e)</b></p>	<p>(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, <u>5 days</u>, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section <del>22974.4, 22978.6, or</del> 22980.3, subdivision (d).</p>	<p>(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be <u>within a range of 0 days, 10 days or</u> to 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section <del>22974.4, 22978.6, or</del> 22980.3, subdivision (a)(2) <u>or subdivision (d)</u>.</p>

Issue Paper Number **12-007**



- ☐ Board Meeting
- ☒ Business Taxes Committee
- ☐ Customer Services and Administrative Efficiency Committee
- ☐ Legislative Committee
- ☐ Property Tax Committee
- ☐ Other

## **Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations 4601, 4603, 4604 and 4605**

### **I. Issues**

Should the Board of Equalization (Board) authorize publication of a new regulation to provide guidelines on the documentation and retention requirements for transfers of cigarettes and tobacco products between retail stores owned by the same legal entity?

In addition, should the Board amend existing regulations to clarify the service requirements when a notice is issued?

Finally, should Board staff be allowed greater flexibility in setting or reducing suspension periods?

### **II. Alternative 1 - Staff Recommendation**

#### ***Item 1 - Proposed Regulation 4801 Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Staff recommends the adoption of proposed Regulation 4801 regarding transfers of cigarettes and tobacco products between retail stores owned by the same legal entity. Adopting the proposed regulation provides Board staff and licensed retailers who own multiple locations with regulatory guidance for satisfying the documentation and invoice requirements required by statute in order to establish the tax-paid status of the product being transferred. See Exhibit 2 for staff's proposed Regulation.

#### ***Item 2 - Regulation 4601 Service of a Notice of Violation or Warning Notice***

Staff recommends amending Regulation 4601 so that the service requirements which presently apply to a Notice of Violation or Warning Notice will apply to any notice issued under the Cigarette and Tobacco Products Licensing Act (Act) and its Regulations. To satisfy the service for all notices, staff proposes amending Regulation 4601 to require that any notice issued under the Act be served in a manner prescribed for the service of a notice of determination, instead of limiting the requirement to the two aforementioned notices. See Exhibit 3 for staff's recommended amendments to Regulation 4601.

#### ***Item 3 - Regulation 4603 Penalties for Licensed or Unlicensed Retailers; Regulation 4604 Penalties for Licensed or Unlicensed Wholesalers and Distributors; and Regulation 4605 Penalties for Licensed or Unlicensed Manufacturers and Importers***

Staff recommends amendments to Regulations 4603, 4604, and 4605 to also allow for a suspension period of five (5) days. The current Regulations allow staff to set or reduce a suspension period to zero (0) days, ten (10) days or twenty (20) days with a maximum suspension period of thirty (30) days. Proposed amendments also include adding references to the Business and Profession Code (B P Code) sections involving violations that mandate the revocation of a license and deletion of references to those B&P Code sections that refer to violations which do not apply to the specific licensee, i.e., retailer, wholesaler, distributor, manufacturer or importer. See Exhibits 4, 5, and 6 for staff's recommended amendments to Regulations 4603, 4604, and 4605.

### **III. Other Alternative(s) Considered**

**Item 1 - Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Consider adopting a Regulation prohibiting the transfer of any cigarettes or tobacco products between retail locations owned by the same legal entity, thereby creating a "bright line" prohibiting transfers as recommended by some Interested Parties.

**Item 2 - Regulation 4601 *Service of a Notice of Violation or Warning Notice***

None considered.

**Item 3 - Regulation 4603 *Penalties for Licensed or Unlicensed Retailers*; Regulation 4604 *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and Regulation 4605 *Penalties for Licensed or Unlicensed Manufacturers and Importers***

Consider adopting staff's original draft recommendation that the regulations be amended to allow staff to set the suspension period between a range of zero (0) days to twenty (20) days or reduce a thirty (30) day suspension to a period within that range thereby providing the greatest degree of flexibility.

## IV. Background

On October 12, 2003, the State of California enacted the Cigarette and Tobacco Products Licensing Act (Assembly Bill 71, Horton [Chapter 890, Statutes 2003]) which established a statewide licensing program under Division 8.6 (commencing with Section 22970) of the B & P Code. The Act imposes licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. Assembly Bill 1749 (Chapter 501, Statutes 2006) added the same licensing requirements to manufacturers and importers of tobacco products. These licensing requirements are in addition to other permits and licenses that may be required depending on a person's business operations. The Act intended to address the problem of untaxed distributions and illegal sales of cigarettes and tobacco products in California and includes provisions for new recordkeeping requirements, identifies violations that may result in license suspensions or revocations including the imposition of civil and criminal penalties, and authorizes Board staff to inspect and seize any untaxed cigarettes or tobacco products. Inspections are performed by the Board's Investigations Division (ID) staff and, based upon the findings during the course of their inspections, may result in the issuance of citations and penalties for violations.

The Act authorizes the Board to administer and enforce the provisions of the Act and to prescribe, adopt, and enforce rules and regulations relating to its administration and enforcement. Since the inception of the Act, the Board has prescribed and adopted regulations to clarify the provisions with the intent to uniformly administer and enforce the provisions of the Act, and to provide guidance and clarity of the Act's provisions to licensed and unlicensed cigarette and tobacco product retailers, wholesalers, distributors, manufacturers, and importers. At the October 1, 2006, Business Taxes Committee meeting, the Board adopted staff's proposed Regulations 4500 and 4501, *Definitions and Citations*; 4502 through 4509, *Licenses – Issuance, Transfer and Denial*; 4600 through 4602, *Notices of Violation or Warning Notices*; 4603 through 4608, *Penalties and Fines*; 4609 and 4700 through 4702, *Appeal Procedures*; and 4703, *Seizure and Forfeiture*. These Regulations were adopted December 12, 2006, and following approval by the State of California's Office of Administrative Law were effective on April 21, 2007. With the exception of an amendment to Regulation 4703, *Seizure and Forfeiture*, to provide for certain exemptions and instances when a licensed distributor may be in possession of un-stamped cigarettes, the Act's Regulations have not been amended or updated.

### **Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Based on recent citations and related appeals proceedings involving the seizure of cigarettes and tobacco products due to a retailer's failure to maintain documentation supporting an assertion that tax-paid product was transferred from one licensed retail location to another licensed retail location owned by the same legal entity, the Special Taxes and Fees Division was asked to develop a new regulation to formalize the Board's existing policies regarding documentation requirements for the transfer of cigarettes and tobacco products between licensed retail locations owned by the same legal entity. Transfers of cigarettes and tobacco products between licensed retail locations owned by the same legal entity excludes sales transactions of cigarettes and tobacco products between licensed retail locations which is expressly prohibited by Revenue and Taxation Code section 30478.

In April 2011, Board staff provided guidance to licensees and staff on its current transfer policies through an update to Publication 78, *Sales of Cigarettes and Tobacco Products in California*, and a letter sent to 1,790 legal entities owning multiple cigarette and tobacco products licensed retail locations. Both the letter and Publication 78 provided that:



“Generally, the transfer of cigarettes and tobacco products are not permitted. However, if you own more than one store and licenses are held by the same legal entity, you may be allowed to transfer cigarettes and tobacco products between stores belonging to the same legal entity. When transferring cigarettes and tobacco products, legible transfer records and copies of the original purchase invoice must be kept at each location involved in the transfer. Such transfer records which must be prepared at the time of transfer, must include the address of each store, the purchase invoice date, the purchase invoice number, the supplier’s name on the invoice, including type of packaging, flavor and or style, and the amounts of items transferred. Failure to provide such documentation when requested can result in the seizure of the claimed transferred product.”

The above guidance represents the basis for the proposed Regulation.

**Regulation 4601 *Service of a Notice of Violation or Warning Notice***

Regulation 4601, *Service of a Notice of Violation or Warning Notice*, adopted December 12, 2006, provides guidance to staff and licensees in regard to the service of the Notice of Violation and Warning Notice. Regulation 4601 was adopted in conjunction with Regulation 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, and instructs staff and licensees that the mailing of the Notice of Violation or Warning Notice to the cited person’s last known address as it appears in the records of the Board will complete delivery of said notice. In lieu of mailing, the notice may be served by personal delivery to the person to be served and shall be deemed complete at the time of such delivery. Since adoption, staff has identified other notices utilized in the administration of the Act and its Regulations that require service. Amendments to Regulation 4601 to provide a uniform service mechanism for all notices required under the Act and its Regulations are recommended for clarity and ease of administration.

**Regulation 4603, *Penalties for Licensed or Unlicensed Retailers*; Regulation 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and Regulation 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

Regulation 4603, *Penalties for Licensed or Unlicensed Retailers*; Regulation 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and Regulation 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*, adopted December 12, 2006, provides staff with guidance regarding the assessment of penalties for a first offense of a violation and for subsequent violations of the Act by a licensed or unlicensed retailer, wholesaler, distributor, manufacturer or importer which would result in the issuance of a Warning Notice, suspension or revocation. Each regulation contains a subdivision that provides that a reduction in the length of a suspension period may be warranted if mitigating circumstances are present as set forth in Regulation 4606. Mitigating circumstances can be determined upon appeal at the Special Tax and Fees Division (which includes the former Excise Taxes Division) or Appeals Division level.

Any violation of the Act may result in either a criminal or civil citation. The Act authorizes the Board to impose civil penalties (suspensions or revocations of a license and/or fines) for violations of the Act. With few exceptions the civil penalties provided in the Act are not mandatory and therefore, the Board has discretion in determining the civil penalties to be imposed. Prior to adoption of these Regulations staff had limited direction in imposing civil penalties of a discretionary nature, making administration of the Act difficult. Staff seeks additional flexibility in setting a suspension period when mitigating circumstances are present to more effectively administer the Act.

## **V. Discussion**

Interested Parties meetings were held on March 6, 2012, and May 4, 2012, to discuss proposed Regulation 4801 and amendments to existing Regulations 4601, 4603, 4604 and 4605 of the Act. Following the March 6, 2012 Interested Parties meeting, Ms. Yvonne Walker, President of SEIU Local 1000 representing the Business Taxes Specialists and Business Taxes Compliance Specialists in the Investigation Division, submitted a letter (Exhibit 11) expressing their concerns with the proposed regulation and amendments to Regulations 4603, 4604 and 4605 that will be discussed below. After the May 4, 2012, Interested Parties meeting, Mr. Scott Louie of Chevron, submitted an email response (Exhibit 12) in support of proposed Regulation 4801 and identified various scenarios that occur on a regular basis that would be adversely affected if a decision was made to prohibit such transfers. Although these were the only two written submittals received, other Interested Parties at both meetings expressed their support or their opposition for the proposed regulation and amendments. Their views and concerns are discussed below.

### ***Proposed Regulation 4801 Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Mr. Steven Alari, representing SEIU, and Mr. Dennis Loper, representing the California Distributors Association, expressed concerns at the meeting on March 6, 2012, that the Act does not provide for such transfers and that each retail location should purchase cigarettes and tobacco products directly from licensed distributors and wholesalers for delivery and sale by that location, thus creating a “bright line” for staff to follow during an inspection of the retail premise. One of the concerns was that adoption of the regulation would create a loophole by allowing retailers to “blend” untaxed tobacco products with products that are tax paid.

Although the Act does not specifically provide for transfers of cigarette and tobacco products between retail locations owned by the same person, the Act does not preclude such transfers either. Mr. Alari acknowledged at the May 4, 2012, Interested Parties meeting that there are no provisions in the Act that specifically preclude transfers. The Act requires that a retailer of cigarettes or tobacco products obtain a retailer’s license for each retail location in which cigarettes or tobacco products are sold, maintain purchase invoices that meet the requirements set forth in section 22978.4 of the B P Code for all cigarettes or tobacco products the retailer purchased for a period of four years and that these records be maintained at the retail location for at least one year after purchase. Section 22978.4 also prescribes form and content requirements for invoices issued by distributors and wholesalers. Besides requiring distributor and wholesaler information, each invoice must contain the name, address and license number of the customer, an itemized listing of cigarette and tobacco products sold, date of sale, and the amount of excise taxes due to the Board by the distributor or a statement that reads: “All California cigarette and tobacco product taxes are included.”

A retail location is defined under section 22971 (q) of the Act as any building from which cigarettes or tobacco products are sold at retail, or a vending machine. “Sale” is defined in Section 30006 of the Revenue and Taxation Code as any transfer of title or possession for consideration, exchange or barter, in any manner or by any means whatever. As a result, the Act does not require a retailer to maintain a license at a warehouse or storage location from which retail sales are not made. The Act also does not require that a distributor or wholesaler deliver only to the address of the licensed retail location. Section 22978.4 (a)(4) requires that a distributor or wholesaler include on any invoice the name, address, and license number of the retailer, distributor, or wholesaler to whom cigarettes or tobacco products are sold. It does not require that the product be delivered to the address where the retail license is held. There would appear to be good reasons for not requiring such a limitation, as had such a requirement been included in the Act, traditional cash and carry purchases would be prohibited, and vending machine operators would only be able to take delivery at the location of a licensed vending

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machine, which is generally located at another person's business. One could therefore make an argument that without such delivery limitations the Act contemplates transfers of cigarettes and tobacco products between retail or storage locations owned by the same legal entity so long as the invoice retention requirements are satisfied at each retail location.

Mr. Scott Louie, on behalf of Chevron, submitted an email response in support of proposed Regulation 4801, and identified a number of scenarios where transfers of cigarettes and tobacco products make prudent business sense, and occur on a regular basis. If retailers were unable to transfer product, business would be negatively impacted. Scenarios identified include delivery delays necessitating transfers from another store to avoid lost sales; supplier is out of stock and again product would need to be transferred from another store; ordering errors resulting in one location being overstocked requiring transfers to another store; sales increase due to an unanticipated event that would deplete one location's stock; and, store closures, abandonments or divestments requiring the transfer of unsold inventory.

Mr. Ron Michelson, owner of two Briar Patch stores, and Ms. Paula Treat, representing the International Premium Cigar and Pipe Retailers, expressed support for proposed Regulation 4801 and saw it as necessary for doing business in a competitive environment. Mr. Michelson's concern was with the difficulty in maintaining the transfer log when it is difficult to identify the invoice associated with the product being transferred and when product transferred is once again transferred. Also he felt that the Regulation included some redundancy with respect to the transfer log or document requirements, such as requiring license information along with location information to be included in the log, in addition to a copy of the invoice which already contains the same information. However, Mr. Michelson acknowledged at the May 4, 2012, Interested Parties meeting that although the documentary requirements of the Regulation place a burden on small businesses, not being able to transfer product between his business locations would be much more problematic.

Staff from our Investigation's Division (ID), in an attempt to address some of these concerns, without weakening or creating a loophole in the proposed Regulation's provisions, prepared an example of an acceptable transfer log (Exhibit 7) that may be used along with a copy of an invoice that would satisfy the documentary requirements of the proposed Regulation. The transfer log prepared by ID included only two transfers and has been expanded to include additional transfer examples to multiple locations and transfers returning product back to the original transferring location. If proposed Regulation 4801 is adopted, the sample transfer log will be made available on the Board's website and in future mailings and publications provided to licensed retailers. In addition, staff recommends proposed Regulation 4801 allow copies of invoices at the receiving location to be maintained on alternative storage media as specified in Regulation 4901 (h), Title 18 of the California Code of Regulations, and require that facilities and equipment to view the storage media be made available at the receiving location. The use of alternative storage media for documenting the original purchase invoice is common practice at many of the national chains that sell cigarettes and tobacco products. Staff believes including this provision is appropriate for consistent application of the documentation requirements currently utilized throughout the industry and allowed by Regulation 4901 as an acceptable means for satisfying the records requirement.

To acknowledge the practice of transfers of cigarettes and tobacco products within this industry, the Board has adopted procedures allowing for the transfers of cigarettes and tobacco products between retail locations owned by the same person. These procedures acknowledge the blending concern and are designed to address them through requirements that copies of invoices be maintained at both locations and a transfer log or document be available detailing the amount of product, description of product, and license information of the transferring and receiving locations. Proposed Regulation 4801 is consistent with current Board policies and procedures and is intended to provide for consistent

enforcement of the documentary requirement provisions. The proposed Regulation will also provide retailers with the documentation and recordkeeping requirements for these types of transfers so as to avoid seizures of the transferred products, along with avoiding citations and fines that may be assessed against the retailer for improper documentation of these transfers.

In regard to blending, unfortunately due to the fungible nature of certain types of tobacco products, one invoice for tax paid product could be used in an attempt to satisfy the invoicing requirements of purchases for tobacco products that were not tax paid. These attempts to evade tax have occurred historically and continue today within this particular industry, primarily with tobacco products because such products are not stamped. As an example, if at the location there is never more inventory than there is tax paid invoice support and the dates of that inventory reconcile with that of the supporting invoices, one would come to the conclusion, without other evidence, that the product on the shelf was tax paid and purchased from a licensed wholesaler or distributor. However, untaxed purchases of the same product from an unlicensed person could be comingled with the tax paid inventory without raising suspicion so long as the shelf stock never exceeds the amount of inventory supported by tax paid invoices.

***Regulation 4601 Service of a Notice of Violation or Warning Notice***

Regulation 4601, adopted December 12, 2006, provides guidance to staff and licensees in regard to the service of the Notice of Violation and Warning Notices. Regulation 4601 was adopted in conjunction with Regulation 4600 *Issuance and Contents of a Notice of Violation or Warning Notice*. Prior to the Interested Parties Meeting of March 6, 2012, staff identified two additional notices -- Notice of Conference and Notice of Decision -- that staff serve as directed by the Act and its Regulations. Staff's initial recommendation was to amend the regulation in order to include similar regulatory guidance for serving a Notice of Suspension and Notice of Revocation. In order to provide staff with uniform guidance and licensees with consistent methods for service of **any and all** notices required under the Act and its Regulations, staff recommends that Regulation 4601 be renamed to *Service of a Notice* and amend to provide that service be the same as that of the service of a Notice of Determination pursuant to Revenue and Taxation Code Section 30206 of the Cigarette and Tobacco Products Tax Law. Referring to Notice of Determination provisions, which is currently included in Regulation 4601, is common practice for stipulating service requirements for "notices" throughout the Revenue and Taxation Code.

***Regulation 4603 Penalties for Licensed or Unlicensed Retailers; Regulation 4604 Penalties for Licensed or Unlicensed Wholesalers and Distributors; and Regulation 4605 Penalties for Licensed or Unlicensed Manufacturers and Importers***

The Act allows the Board, in addition to any applicable fines or penalties for a violation of the licensing provisions, upon the first finding of a violation by a licensee, to suspend a license for **up to** 30 days, pursuant to Section 22980.3(a)(1). Upon the effective date of the suspension, the licensee shall immediately cease the sale of cigarettes and/or tobacco products until completion of the suspension period. Licensees are typically notified of the suspension period by mail at least three weeks prior to the beginning of the suspension period. This Notice of Suspension includes detailed instructions for complying with the terms of the suspension and includes additional copies of the suspension notice for posting pursuant to Section 22980.5. Once a Notice of Suspension is mailed, staff follows up the notification by telephone to make sure the mailer has been received.

In April 2006, Regulations 4603, 4604, and 4605 were adopted to provide guidance regarding the assessment of penalties for a first offense of a violation and for subsequent violations of the Act by a licensed or unlicensed retailer, wholesaler, distributor, manufacturer or importer which would result in the issuance of a Warning Notice, suspension or revocation. Each regulation provides that a reduction

in the length of a suspension period may be warranted if mitigating circumstances are present as set forth in Regulation 4606. Mitigating circumstances can be determined upon appeal at the Special Tax and Fees Division (which includes the former Excise Taxes Division) or Appeals Division level.

Pursuant to Regulation 4606, factors including, but not limited to, the following may be considered for purposes of determining whether mitigating circumstances exist to warrant a reduction in the length of a suspension period:

- (a) How recently the licensee purchased the business or began operations and acquired inventory of cigarettes and/or tobacco products.
- (b) The amount of cigarettes without stamps and with counterfeit tax stamps in relation to the size of the licensee's overall inventory.
- (c) The size of the licensee's cigarette and/or tobacco product business.
- (d) The retail value of any cigarettes or tobacco products seized.
- (e) An absence of prior seizures.

If a suspension period is reduced due to mitigating circumstances, current regulations only allow the reduction of a suspension period to be set at: 0 days, 10 days or 20 days.

Concerns were expressed at the Interested Parties meeting on March 6, 2012, by Mr. Dennis Loper, representing the California Distributor's Association, and Mr. Steven Alari of SEIU, who were opposed to additional flexibility in setting the period of suspension within a range of 1 to 20 days. An argument was made that the minimum number of days of suspension should remain at 10 as it is a deterrent and allows ID staff sufficient time to inspect 100 percent of those serving a suspension period. ID currently inspects 100 percent of the retail locations at some point during their suspension period. In addition, any shorter period could put the wholesalers and distributors in jeopardy of violating the law by selling to someone during a short suspension period. Presumably certain wholesalers or distributors would not have the ability to cease selling cigarettes or tobacco products to retailers serving a short suspension period. It was further noted that Board costs could increase if a shorter suspension period were allowed due to the increased number of suspensions (Note: the increased number of suspensions cited is based on an estimated number of accounts that would serve a reduced suspension instead of having their suspension reduced to 0 days). Mr. Loper suggested that they would possibly support reducing the suspension period if mitigating circumstances are delineated and dollar values of cigarettes or tobacco products are assigned to days.

In the second discussion paper, discussed at the May 4, 2012 Interested Parties meeting, staff recommended alternate language eliminating the range of days, and agreed to propose 5 day suspension period in addition to the current 10, 20 or 30 day suspension periods. It was believed, that a 5 day suspension period would strike an appropriate balance and satisfy the concerns expressed by Mr. Alari and Mr. Loper and still provide staff with the flexibility in administering the Act. Although Mr. Loper was not in attendance, Mr. Alari was, and appeared to be satisfied with the 5 day period as it provided ID with the time necessary to perform an inspection.

Wholesalers and distributors currently receive email notice from the Board at least two weeks prior to the suspension period when any licensee is suspended for 10, 20 or 30 days. Email notices are also sent out listing the names and effective dates of licenses to be revoked. Staff believes that the current recommendation to amend the Regulations to allow for a minimum of 5 days for a suspension period should not further jeopardize a wholesaler or distributor's ability to cease selling during a period of suspension.

During the period of March 2009 through October 2011 (32 months), 546 appeals were heard by staff at the first level appeal of a violation of the Act that could result in up to a 30 day suspension. Based on these appeals, staff reduced the suspension period in 240 instances to zero days based on mitigating circumstances and in two instances recommended no penalty. The remaining 304 appeals resulted in a 10 day, 20 day or 30 day suspension. Staff believes that had a 5 day suspension period been available, that many of these appeal cases, where staff reduced the suspension period to 0 days, may have resulted in a 5 day suspension. First level appeals staff in Special Taxes and Fees believe a 10 day suspension in many instances is too harsh based on the value of cigarette and tobacco products seized or the materiality of the seizure in terms of the taxpayer's business operations and given the circumstances in these cases are more likely to impose a 0 day suspension. Staff holding the appeals conferences believe a 5 day suspension may be more fitting of the violation in many of these instances. A 5 day suspension from selling cigarette and tobacco products is still a strong deterrent for any retailer who is in the business of selling these products. Staff has also confirmed that a 5 day suspension period provides adequate time needed by ID to visit the location and confirm compliance with the suspension. In addition, the added workload of potentially 3 to 4 additional inspections a month would be absorbable based on current staffing.

Staff believes setting suspension periods by further delineating or attempting to establish specific criteria for identifying when mitigating circumstances are present would set too rigid of a guideline. The circumstances pertaining to each appeal are so varied that efforts to describe and allocate them across a 0 to 10 day range of suspension periods would be difficult at best especially in terms of crafting distinguishing and compelling differentiations for suspension periods that may be only one day longer than another. Staff was seeking additional discretion for the first and second level hearing officers when setting periods of suspension, specifically between the 0 day to 10 day range, not more rigidity when administering the Act.

Although it is now staff's recommendation to amend the Regulations by adding a 5 day suspension period for the reasons cited above, for the Board's consideration, the original proposal for a 0 day to 20 day range remains as an alternative for consideration (Exhibits 8, 9, and 10). As initially proposed this alternative provides the hearing officers with the greatest degree of flexibility when setting a suspension period, but would create challenges for ID to schedule inspections where the suspension period is only 1 to 3 days and could lead to some locations not being inspected during their suspension period.

Both staff's recommendation and the alternative language include adding references to the B&P Code sections involving violations that mandate the revocation of a license and deletion of references to those B P Code sections that refer to violations which do not apply to the specific licensee, i.e., retailer, wholesaler, distributor, manufacturer or importer.

## **VI. Alternative 1 - Staff Recommendation**

### **Item 1 – Adopt Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the same Person***

#### **A. Description of Alternative 1**

Regulation 4801 as proposed by staff formalizes the Board's current policy of allowing transfers of cigarettes and tobacco products between retail stores owned by the same legal entity. It requires that every retailer of cigarettes and tobacco products maintain purchase invoices for all cigarettes and tobacco products purchased and to make those invoices available for inspection by the Board or

law enforcement. Licensed retailers owning more than one location may transfer product between locations so long as the retailer prepares a transfer log or other document at the time of transfer and maintains a copy of the transfer log at both the transferring and receiving location along with copies of applicable invoices. These records must be maintained for a period of four years with copies of the log and invoices maintained at each location involved in the transfer for a period of one year. Copies of invoices may be maintained on alternative storage media pursuant to Regulation 4901 *Records*. Facilities and equipment must be provided for reading, locating and reproducing any invoices maintained on alternative storage media.

The transfer log or document shall show the following:

- (1) The transferring retail location, license information, supplier's name, invoice number, and date the bulk cigarettes and tobacco products was made;
- (2) The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and
- (3) An itemized listing of cigarettes and tobacco products transferred.

#### **B. Pros of Alternative 1**

- Consistent with the Board's current policy on transfers.
- Provides regulatory support and guidance to taxpayers and staff.
- Adopts into regulation the retail industry's current business practices regarding transfers between retail stores owned by the same legal entity.

#### **C. Cons of Alternative 1**

- Requires a degree of additional verification during an inspection.
- Requires a taxpayer to prepare and maintain an additional document or log to satisfy the records requirement in section 22974 of the B P Code.

#### **D. Statutory or Regulatory Change for Alternative 1**

No statutory change is required. However, staff's recommendation does require adoption of proposed Regulation 4801.

#### **E. Operational Impact of Alternative 1**

Minor. Although the regulation adopts current policy, staff intends to add the sample transfer log to the Board's website and in appropriate publications for the tobacco industry.

#### **F. Administrative Impact of Alternative 1**

##### **1. Cost Impact**

Absorbable.

##### **2. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).

**G. Taxpayer/Customer Impact of Alternative 1**

None, adopts current policy.

**H. Critical Time Frames of Alternative 1**

None.

**Item 2 – Adopt staff’s proposed amendments to Regulation 4601 *Service of a Notice of Violation or Warning Notice***

**A. Description of Alternative 1**

Proposed amendments to Regulation 4601 provide staff with a consistent method for service for all notices required under the Act and its regulations. Issuance of notices shall be served personally or by mail in the manner prescribed for the service of a notice of determination under Revenue and Taxation Code section 30206, which stipulates that a notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute or other facility regularly maintained or provided by the United States postal Service, without extension of time for any reason.

**B. Pros of Alternative 1**

- Provides Board staff administering the Act with regulatory support for the service of any notice under the Act.
- Incorporates the Board’s standard service requirements for the serving of any notice under the Act.
- Is consistent with the serving of most notices issued under the R T Code.
- Referencing the Service of a Notice of Determination under the R T Code provides efficient administration should changes be required to standard service requirements.

**C. Cons of Alternative 1**

None.

**D. Statutory or Regulatory Change for Alternative 1**

No statutory change is required. However, staff’s recommendation does require adoption of proposed amendments to Regulation 4601.

**E. Operational Impact of Alternative 1**

None, incorporates the Board’s current service requirements.

**F. Administrative Impact of Alternative 1**

**3. Cost Impact**

None

**4. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).



### **G. Taxpayer/Customer Impact of Alternative 1**

None, incorporates the Board's current service requirements.

### **H. Critical Time Frames of Alternative 1**

None.

## ***Item 3 - Regulation 4603 Penalties for Licensed or Unlicensed Retailers; Regulation 4604 Penalties for Licensed or Unlicensed Wholesalers and Distributors; and Regulation 4605 Penalties for Licensed or Unlicensed Manufacturers and Importers***

### **A. Description of Alternative 1**

The proposed amendments to Regulations 4603, 4604 and 4605 provide staff with an option of imposing a 5 day suspension period in addition to being able to impose a 0 day, 10 day or 20 day suspension period when mitigating circumstances are present. In addition, each regulation is amended to include statutory citations resulting in mandatory revocations. In particular a mandatory revocation for a second violation for possession of untaxed cigarettes or tobacco products applies only to retailers, wholesalers and distributors, and a mandatory revocation for continued sales or gifting of cigarettes or tobacco products during a period of suspension applies to retailers, wholesalers, distributors, manufacturers and importers. Amendments also delete certain statutory sections that do not apply to the pertinent license.

### **B. Pros of Alternative 1**

- Provides staff with an added option of a 5 day suspension when the level of violation does not warrant a 10 day suspension.
- Provides staff with requested flexibility in administering the Act.
- Allows sufficient time for ID to re-inspect the retail store during a period of suspension.
- A 5 day suspension period is still punitive and an adequate deterrent.
- Properly identifies violations mandating revocations.

### **C. Cons of Alternative 1**

- May result in an increase in the number of inspections.

### **D. Statutory or Regulatory Change for Alternative 1**

No statutory change is required. However, staff's recommendation does require adoption of proposed amendments to Regulations 4603, 4604, and 4605.

### **E. Operational Impact of Alternative 1**

May result in additional inspections.

### **F. Administrative Impact of Alternative 1**

#### **5. Cost Impact**

None, potential increase to the number of inspections is absorbable.

#### **6. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).

### **G. Taxpayer/Customer Impact of Alternative 1**

Taxpayers who violate the Act may receive a 5 day suspension period in addition to the current 0 day, 10 day and 20 day suspension periods when mitigating circumstances are present.

### **H. Critical Time Frames of Alternative 1**

None.

## **VII. Other Alternatives**

### **Item 1 - Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

#### **A. Description of Alternative**

Consider prohibiting transfers of cigarettes and tobacco products between retail stores regardless of ownership.

#### **B. Pros of Alternative**

- Limits the invoice documentation required on site to only those invoices referencing the licensed retail location.
- Prohibition creates a “bright line” on transfers for retailers and Board staff to follow.

#### **C. Cons of Alternative**

- Eliminates a retailer’s ability to transfer product to their own stores regardless of the business situation. For instance, transferring product from a closed store to one that is still in business; one store has over bought a product that can be sold at another location; supplier is out of a product that is available at another taxpayer owned location, or delays in delivering a product to one retail store whereas the product is available at another taxpayer owned location.
- Prohibition may prevent taxpayers with multiple locations from taking advantage of quantity discounts.

#### **D. Statutory or Regulatory Change for Alternative**

No statutory change required. However, since the Act does not specifically prohibit the transfer of cigarettes and tobacco products between retail stores owned by the same legal entity, a regulation prohibiting transfers should be considered.

#### **E. Operational Impact of Alternative**

Prohibiting transfers would require the Board to rescind the letter mailed April 2011 to retailers owning multiple locations that addressed the current policy allowing transfers. Revise Publication 78 *Sales of Cigarettes and Tobacco Products in California*, and advise of the policy change in other outreach materials to the industry.

#### **F. Administrative Impact of Alternative**

##### **1. Cost Impact**

Additional mailing costs unknown.

##### **2. Revenue Impact**

None.

**G. Taxpayer/Customer Impact of Alternative**

A prohibition of the common practice of transferring cigarettes or tobacco products between at taxpayer's own stores could have a major impact on those retailers operating multiple licensed locations.

**H. Critical Time Frames of Alternative**

None.

**Item 2 - Proposed amendments to Regulation 4601 *Service of a Notice of Violation or Warning Notice***

**A. Description of Alternative**

None considered.

**B. Pros of Alternative**

None.

**C. Cons of Alternative**

None.

**D. Statutory or Regulatory Change for Alternative**

None.

**E. Operational Impact of Alternative**

None.

**F. Administrative Impact of Alternative**

**1. Cost Impact**

None.

**2. Revenue Impact**

None.

**G. Taxpayer/Customer Impact of Alternative**

None.

**H. Critical Time Frames of Alternative**

None.

**Item 3 - Regulation 4603 *Penalties for Licensed or Unlicensed Retailers*; Regulation 4604 *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and Regulation 4605 *Penalties for Licensed or Unlicensed Manufacturers and Importers***

**A. Description of Alternative**

Adopt staff's original draft amendments to Regulations 4603, 4604 and 4605 which provided staff with a *range of 0 days to 20 days* for setting a suspension period when mitigating circumstances are present. Adopt all other amendments recommended by staff adding the statutory citations mandating a revocation and delete those that do not apply to the individual licensee..

**B. Pros of Alternative**

- Provides staff with the greatest degree of flexibility in setting a suspension period when mitigating circumstances are present.
- May result in staff issuing one or two day suspension periods in lieu of 0 days.

**C. Cons of Alternative**

- For short suspension periods, may prevent ID from inspecting the retail store during the period of suspension.
- For short suspension periods, may not allow sufficient time for wholesalers and distributors to prevent sales of cigarettes and tobacco products to the licensee during a period of suspension.

**D. Statutory or Regulatory Change for Alternative**

No statutory change required. However, does require adopting the alternative amendments to Regulations 4603, 4604, and 4605.

**E. Operational Impact of Alternative**

May result in additional inspections.

**F. Administrative Impact of Alternative**

**1. Cost Impact**

Additional inspections are absorbable. .

**2. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).

**G. Taxpayer/Customer Impact of Alternative**

Taxpayers may receive a one or two day suspension period in lieu of a zero day suspension period when mitigating circumstances are present.

**H. Critical Time Frames of Alternative**

None.

**Preparer/Reviewer Information**

Prepared by: Policy and Compliance Division, Property and Special Taxes Department

Current as of: June 6, 2012

REVENUE ESTIMATE

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION



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**Proposed Regulation 4801 and Amendments to Cigarette and Tobacco Products Licensing Act Regulations 4601, 4603, 4604 and 4605**

**I. Issues**

Should the Board of Equalization (Board) authorize publication of a new regulation to provide guidelines on the documentation and retention requirements for transfers of cigarettes and tobacco products between retail stores owned by the same legal entity?

In addition, should the Board amend existing regulations to clarify the service requirements when a notice is issued?

Finally, should Board staff be allowed greater flexibility in setting or reducing suspension periods?

**II. Alternative 1 - Staff Recommendation**

***Item 1 - Proposed Regulation 4801 Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Staff recommends the adoption of proposed Regulation 4801 regarding transfers of cigarettes and tobacco products between retail stores owned by the same legal entity. Adopting the proposed regulation provides Board staff and licensed retailers who own multiple locations with regulatory guidance for satisfying the documentation and invoice requirements required by statute in order to establish the tax-paid status of the products being transferred. See Exhibit 2 for staff's proposed Regulation.

***Item 2 - Regulation 4601 Service of a Notice of Violation or Warning Notice***

Staff recommends amending Regulation 4601 so that the service requirements which presently apply to a Notice of Violation or Warning Notice will apply to any notice issued under the Cigarette and Tobacco Products Licensing Act (Act) and its Regulations. To satisfy the service for all notices, staff proposes amending Regulation 4601 to require that any notice issued under the Act be served in a manner prescribed for the service of a notice of determination, instead of limiting the requirement to the two aforementioned notices. See Exhibit 3 for staff's recommended amendments to Regulation 4601.

**Item 3 - Regulation 4603 *Penalties for Licensed or Unlicensed Retailers; Regulation 4604 Penalties for Licensed or Unlicensed Wholesalers and Distributors; and Regulation 4605 Penalties for Licensed or Unlicensed Manufacturers and Importers***

Staff recommends amendments to Regulations 4603, 4604, and 4605 to also allow for a suspension period of five (5) days. The current Regulations allow staff to set or reduce a suspension period to zero (0) days, ten (10) days or twenty (20) days with a maximum suspension period of thirty (30) days. Proposed amendments also include adding references to the Business and Profession Code (B P Code) sections involving violations that mandate the revocation of a license and deletion of references to those B P Code sections that refer to violations which do not apply to the specific licensee, i.e., retailer, wholesaler, distributor, manufacturer or importer. See Exhibits 4, 5, and 6 for staff's recommended amendments to Regulations 4603, 4604, and 4605.

### **III. Other Alternative(s) Considered**

**Item 1 - Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Consider adopting a Regulation prohibiting the transfer of any cigarettes or tobacco products between retail locations owned by the same legal entity, thereby creating a "bright line" prohibiting transfers, as recommended by some interested parties.

**Item 2 - Regulation 4601 *Service of a Notice of Violation or Warning Notice***

None considered.

**Item 3 - Regulation 4603 *Penalties for Licensed or Unlicensed Retailers; Regulation 4604 Penalties for Licensed or Unlicensed Wholesalers and Distributors; and Regulation 4605 Penalties for Licensed or Unlicensed Manufacturers and Importers***

Consider adopting staff's original draft recommendation that the regulations be amended to allow staff to set the suspension period between a range of zero (0) days to twenty (20) days or reduce a thirty (30) day suspension to a period within that range, thereby providing the greatest degree of flexibility.

## **Background, Methodology, and Assumptions**

### **Alternative 1 – Staff Recommendation**

**Item 1:** There is nothing in Item 1 of the staff recommendation that would impact revenue. Regulation 4801 as proposed by staff formalizes the Board's current policy of allowing transfers of cigarettes and tobacco products between retail stores owned by the same legal entity. It requires that every retailer of cigarettes and tobacco products maintain purchase invoices for all cigarettes and tobacco products purchased and to

make those invoices available for inspection by the Board or law enforcement. Licensed retailers owning more than one location may transfer product between their licensed locations so long as the retailer prepares a transfer log or other document at the time of transfer and maintain a copy of the transfer log at both the transferring and receiving location along with copies of applicable invoices. These records must be maintained for a period of four years with copies of the log and invoices maintained at each location involved in the transfer for a period of one year. Copies of invoices may be maintained on alternative storage media pursuant to Regulation 4901 *Records*. Facilities and equipment must be provided for reading, locating and reproducing any invoices maintained on alternative storage media.

**Item 2:** There is nothing in Item 2 of the staff recommendation that would impact revenue. The proposed amendments to Regulation 4601 provide staff with the method for service for all notices required under the Act and its regulations. Issuance of notices shall be served personally or by mail in the manner prescribed for the service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law. This section stipulates that a notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason.

**Item 3:** There is nothing in Item 3 of the staff recommendation that would impact revenue. Staff's proposed amendments to Regulations 4603, 4604 and 4605, provide staff with an option of imposing a 5 day suspension period in addition to being able to impose a 0 day, 10 day or 20 day suspension period when mitigating circumstances are present. In addition, each regulation is amended to include statutory citations resulting in mandatory revocations, i.e., upon second violation for possession of untaxed cigarettes or tobacco products, which only applies to retailers, wholesalers and distributors, and continued sales or gifting of cigarettes or tobacco products during a period of suspension, which applies to retailers, wholesalers, distributors, manufacturers and importers. Amendments also delete certain statutory sections that do not apply to the pertinent license.

#### **Other Alternative(s) Considered**

**Item 1:** There is nothing in Item 1 of the other alternative(s) considered that would impact revenue. This alternative would consider prohibiting transfers of cigarettes and tobacco products between retail stores regardless of ownership.

**Item 2:** There is nothing in Item 2 of the other alternative(s) considered that would impact revenue. There were none considered.

**Item 3:** There is nothing in Item 3 of the other alternative(s) that would impact revenue. This alternative recommends adopting staff's original draft amendments to Regulations 4603, 4604 and 4605 which provided staff with a range of 0 days to 20

days for setting a suspension period when mitigating circumstances are present. All other recommended amendments adding the statutory citations mandating a revocation and deleting those that do not apply to the individual licensee remain the same.

## **Revenue Summary**

### **Alternative 1:**

Item 1 – This alternative does not have a revenue impact.

Item 2 – This alternative does not have a revenue impact.

Item 3 – This alternative does not have a revenue impact.

### **Other alternatives considered:**

Item 1 – This alternative does not have a revenue impact.

Item 2 – This alternative does not have a revenue impact.

Item 3 – This alternative does not have a revenue impact.

## **Preparation**

Mr. Bill Benson, Jr., Acting Chief, Research and Statistics Section, Legislative and Research Division, prepared this revenue estimate. Ms. Lynn Bartolo, Chief, Special Taxes, Policy and Compliance Division, Property and Special Taxes Department, reviewed this revenue estimate. For additional information, please contact Mr. Benson at 916-445-0840.

June 1, 2012



**DRAFT – Proposed Regulation 4801**

Transfers of Cigarettes and Tobacco Products Between Retail Stores Owned by the Same Person.

*Reference:* Section 22971, 22974, 22974.3, and 22978.4, Business and Professions Code

(a) GENERAL. Every retailer of cigarettes and tobacco products is required to maintain purchase invoices for all cigarettes and tobacco products purchased and make those invoices available for inspection by the Board or a law enforcement agency. A licensed retailer owning multiple locations who wishes to transfer cigarettes and tobacco products between its licensed locations shall prepare a transfer log or document at the time of transfer and maintain the records for four years from the date of transfer. A copy of the transfer log or document, accompanied by a copy of the original purchase invoice(s) documenting the purchase of each item transferred, must be kept at both the transferring and receiving locations involved in the transfer for at least one year after the transfer. Copies of original purchase invoices may be maintained at the receiving location on alternative storage media as prescribed in Regulation 4901 (h). The taxpayer must provide facilities and equipment for reading, locating, and reproducing any invoices maintained on alternative storage media.

(b) SPECIFIC APPLICATION. The transfer log or document shall show the following:

- (1) The transferring retail location, license information, supplier's name, invoice number, and the date the bulk cigarettes and tobacco products purchase was made;
- (2) The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and,
- (3) A legible itemized listing of cigarettes and tobacco products transferred including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.

(c) The transfer of cigarettes and tobacco products shall only be allowed when the legal entity licensed as the retailer for the retail location transferring the cigarettes and tobacco products is the same legal entity that is licensed as the retailer at the retail location receiving the cigarettes and tobacco products. As an example, a transfer between a location licensed as a sole proprietorship and a location licensed as a partnership where the sole proprietor is one of the partners would not qualify under this section since the same legal entity does not own both locations.

(d) Records of the transfer shall be made available to the Board or its authorized representative for examination upon request. Failure to provide such documentation when requested can result in the seizure of the cigarettes or tobacco products that are claimed to be transferred and the issuance of a citation. Transfer logs or documents created or provided after a seizure and/or citation are not acceptable and cannot be used for the return of seized product or dismissal of a violation.

**Proposed Amendments Regulation 4601, Service of a Notice of Violation or Warning Notice**

*Reference: Sections 22974.7, 22978.7, 22979.7, Business and Professions Code.*

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law. ~~The Notice of Suspension, Notice of Revocation, Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.~~

## Proposed Amendments Regulation 4603, Penalties for Licensed or Unlicensed Retailers

*Reference:* Sections 22973, subdivision (a)(5), 22974, 22974.3, 22974.4, 22974.7, 22980.1, subdivisions (c), (d), (e), (g), 22980, subdivision (b), 22980.2, subdivision (a), 22980.3, subdivisions (a)(2), (d), Business and Professions Code.

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).
- (2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision (b)).
- (4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

- (1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).
  - (2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).
- (c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.
- (d) A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:
- (1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.
  - (2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.
  - (3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.
  - (4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, ~~22978.6~~, or 22980.3, subdivision (a)(2) or subdivision (d).

## **Proposed Amendments Regulation 4604, Penalties for Licensed or Unlicensed Wholesalers and Distributors**

*Reference:* Sections 22974.7, 22977, subdivision (a)(5), 22978.1, 22978.2, ~~22978.7~~, 22978.5, subdivision (b), ~~22978.7~~, 22979.7, 22980, subdivision (b), 22980.1, subdivisions (b), (c), (d), (e), (f), (g), 22980.2, subdivision (a), and 22980.3, subdivisions (a)(2), (d), Business and Professions Code.

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).

(2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).

(3) Business and Professions Code section 22978.5, subdivision (b) (distributor's or wholesaler's failure to retain sales records).

(4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

**(b)** A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision. (b)).

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

**(d)** A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

**(e)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4~~, 22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

## Proposed Amendments Regulation 4605, Penalties for Licensed or Unlicensed Manufacturers and Importers

*Reference:* Sections 22974.7, ~~22978.7~~, ~~22979.4~~, 22979, subdivision (b)(1), ~~22979.4~~, 22979.5, subdivision (b), ~~22979.6~~, subdivision (c), 22979.7, 22980.1, subdivisions (a), (e), (f), 22980.2, subdivision (a), ~~22979.6~~, ~~subdivision (e)~~, ~~22980.3~~ subdivision (a)(2), (d), Business and Professions Code.

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).
- (2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).
- (3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).
- (4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).
- (6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

(b) A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. Tax. Code, § 30163, subdivision. (b)) shall result in a 20-day suspension.

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

(d) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4~~, ~~22978.6~~, ~~or~~ 22980.3, subdivision (a)(2) or subdivision (d).

**Sample Transfer Log  
Cigarettes and Tobacco Products**

<b>Store Transferring Product</b>	<b>Store Receiving Product</b>	<b>Date of Transfer</b>	<b>Items Transferred</b>	<b>Original Purchase From</b>
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	B Street Market 123 B Street Anywhere, CA LRQ 91-1XXXXX	March 2, 2010	50 packs Marlboro cigarettes, 100 5 boxes Romeo y Juliet Cigars (25 ea)	LD Tobacco Distributors LDG 90-2XXXXX February 14, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	B Street Market 123 B Street Anywhere, CA LRQ 91-1XXXXX	April 30, 2010	7 rolls Grizzly Long Cut, Mint (5ea) 2 packs Black & Mild cigars, wine flavor (5ea) 3 packs Black & Mild cigars, wine flavor, wood tip (5 ea)	S&W Wholesale SWQ 90-3XXXXX April 27, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	D Street Market 123 D Street Anywhere, CA LRQ 91-3XXXXX	June 28, 2010	50 packs Marlboro Cigarettes Red King 12 packs Backwoods Sweet (6ea) 6 rolls Copenhagen Regular (5ea)	Tobacco Road Distributors SWQ 90-4XXXXX June 12, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	C Street Market 123 C Street Anywhere, CA LRQ 91 2XXXXX	August 15, 2010	8 packs Swisher Cigarillo wood tip (5ea) 10 boxes Salem Gold 100	S&W Wholesale SWQ 90-3XXXXX July 21, 2010
D Street Market 123 D Street Anywhere, CA LRQ 91-3XXXXX	A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	August 28, 2010	6 packs Backwoods Sweet (6ea)	Tobacco Road Distributors SWQ 90-4XXXXX June 12, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	E Street Market 123 E Street Anywhere, CA LRQ 91 4XXXXX	October 3, 2010	20 packs Marlboro Cigarettes Gold 100 2 rolls Skoal Long Cut Mint (5ea) 2 rolls Skoal Bandit Wintrg. (5ea)	LD Tobacco Distributors LDG 90-2XXXXX September 29, 2010

**Note:** Transfer of cigarettes and tobacco products is allowed only when the legal ownership (as registered with the BOE) of the store transferring the product is the same as the legal ownership of the store receiving the product.

**For example:**

<b>Store Transferring Product</b>	<b>Store Receiving Product</b>	<b>Is the Transfer Allowed?</b>
John Smith –sole proprietor	John Smith – sole proprietor	Yes
John Smith – sole proprietor	John Smith – corporate officer	No
John Smith – sole proprietor	John Smith – partner	No

**Alternate - Amendments Regulation 4603, Penalties for Licensed or Unlicensed Retailers**

*Reference:* Sections 22973, subdivision (a)(5), 22974, 22974.3, 22974.4, 22974.7, 22980.1, subdivisions (c), (d), (e), (g), 22980, subdivision (b), 22980.2, subdivision (a), 22980.3, subdivisions (a)(2)(d), Business and Professions Code.

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).

(2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(4) Business and Professions Code section 22980.2 subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be within a range of 0 days, 10 days, or to 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).



## **Alternate Amendments Regulation 4604, Penalties for Licensed or Unlicensed Wholesalers and Distributors**

*Reference:* Sections 22974.7, 22977, subdivision (a)(5), 22978.1, 22978.2, ~~22978.7~~, 22978.5, subdivision (b), ~~22978.7~~, 22979.7, 22980, subdivision (b), 22980.1, subdivisions (b), (c), (d), (e), (f), (g), 22980.2, subdivision (a), and 22980.3, subdivisions (a)(2), (d) Business and Professions Code.

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).

(2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's (3) Business and Professions Code section 22978.5, subdivision (b) (distributor's or wholesaler's failure to retain sales records).

(4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

**(b)** A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

**(d)** A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

**(e)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be within a range of 0 days, ~~10 days,~~ or to 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4~~, 22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

## Alternate Amendments Regulation 4605, Penalties for Licensed or Unlicensed Manufacturers and Importers

*Reference:* Sections 22974.7, ~~22978.7~~, ~~22979.4~~, 22979, subdivision (b)(1), 22979.4, 22979.5, subdivision (b), 22979.6, subdivision (c), 22979.7, 22980.1, subdivisions (a), (e), (f), 22980.2, subdivision (a), ~~22979.6, subdivision (c)~~, 22980.3 subdivision (a)(2)(d), Business and Professions Code.

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).

(2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).

(3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).

(4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

(b) A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. Tax. Code, § 30163, subd. (b)) shall result in a 20-day suspension.

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

(d) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be within a range of 0 days, 10 days or to 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4, 22978.6, or 22980.3~~, subdivision (a)(2) or subdivision (d).

Formal Issue Paper 12-007  
SEIU Local 1000 Submittal



March 20, 2012

The Honorable Betty Yee  
Chair, Business Taxes Committee  
Board of Equalization  
450 N Street  
Sacramento, CA 95814

YVONNE R. WALKER  
President

M. CORA OKUMURA  
Vice President  
and Secretary-Treasurer

TAMEKIA ROBINSON  
Vice President  
for Organizing/Representation

MARGARITA MALDONADO  
Vice President for Bargaining

**Re: Cigarette and Tobacco Products Licensing Act**

Chairwoman Yee:

SEIU Local 1000, representing the Business Taxes Specialists and Business Taxes Compliance Specialists in the Investigation Division at the Board of Equalization, writes to inform you of our concerns regarding the proposed new regulations and amendments to the Cigarette and Tobacco Products Licensing Act. The new regulations would allow for the transfer of cigarette and tobacco products between retail stores owned by the same legal entity.

Local 1000 believes that each retail location should purchase cigarette and tobacco products directly from licensed distributors and wholesalers only. This would ensure that California excise taxes are paid and that there would be no confusion as to which retailers have paid taxes and which have not. The new regulations would also create a loophole by allowing retailers to "blend" cigarette and tobacco products, essentially mixing products in which taxes were paid, with those in which taxes were not paid. This makes it nearly impossible to ensure that taxes are paid on all cigarette and tobacco products, as required by law.

SERVICE EMPLOYEES  
INTERNATIONAL UNION

1808 14th Street  
Sacramento, CA 95811  
(916) 554-1200  
(866) 471-SEIU (7348)  
(916) 554-1275 (fax)  
www.seiu1000.org

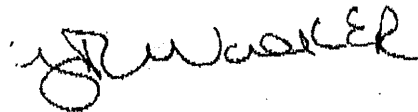


The Honorable Betty Yee  
Re: Cigarette and Tobacco Products Licensing Act  
March 21, 2012  
Page 2 of 2

We also oppose the amendment of Regulations 4603, 4604 and 4605, which would shorten the period of suspension for violation of the California Cigarette and Tobacco Products Licensing Act. We believe that there should be a strong deterrent to those whom have been found in violation of this Act and the current regulations which give the Special Taxes and Fees Division the option of a 20-day, 10-day or zero day suspension, appropriate for such violations.

Thank you for your consideration. I look forward to speaking with you soon.

Sincerely,



Yvonne R. Walker  
President

cc: Honorable Jerome E. Horton, Fourth District  
Honorable Michelle Steel, Third District  
Senator George Runner (Ret.), Second District  
Honorable John Chiang, State Controller, c/o Ms. Marcy Jo Mandel

Bishop, Phil

---

**From:** Louie, Scott (ScottLouie) [ScottLouie@chevron.com]  
**Sent:** Thursday, May 17, 2012 10:50 AM  
**To:** Bishop, Phil  
**Cc:** Retz, David (dret); Serafino, Brian (Brian.Serafino)  
**Subject:** FW: UPDATE- BOE - Business Taxes Committee Material - Cigarette and Tobacco Products Licensing Act Regulations-June2012

**Importance:** High

Phil,

Per our conversation on Monday, here is a list of our retail operations concerns with the tobacco distributor's lobby push to not allow store to store transfers by one legal entity: Please let me know if you have any questions, need anything in addition or would like to discuss. Thanks for reaching out and giving us an opportunity to opine on the issue.

**Scott Louie**

Specialist, State Tax Compliance

**Chevron**

Finance Shared Services, Excise Tax  
2003 Diamond Blvd. Concord, CA 94520  
Tel 925 827 6286  
Fax 925 827 6902

<mailto:ScottLouie@Chevron.com>

If the BOE prohibits the transfer of tobacco products from one legal entity to another, it will negatively impact our business and could result in lost sales. Having the flexibility to transfer from one store to another allows us to respond to different scenarios that occur on a regular basis.

Some of these scenarios include:

1. Delivery problems associated with transportation delays or problems with Auto Ordering, they will need to transfer product IN from another store to avoid lost sales
2. Supplier is Out Of Stock, site would need to transfer product IN until product is available
3. Ordering error causing site to be over stocked, site would need flexibility to transfer product OUT
4. Sales increase due to an unanticipated event
5. For store Closures, Abandonments or Divestments, tobacco transfers are needed to deplete product that was unable to be sold, otherwise it would need to be written off.

Please advise of next steps and / or outcome. Thanks

1           BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION

2                           450 N STREET

3                           SACRAMENTO, CALIFORNIA

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8                           REPORTER'S TRANSCRIPT

9                           JUNE 26, 2012

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15                           BUSINESS TAXES COMMITTEE

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27                           REPORTED BY: Kathleen Skidgel

28

CSR NO. 9039

1

1 P R E S E N T

2

3 For the Committee: Betty T. Yee  
Chair

4

5 Michelle Steel  
Member

6

7 Jerome E. Horton  
Member

8

9 George Runner  
Member

10

11 Marcy Jo Mandel  
12 Appearing for John  
Chiang, State Controller  
13 (per Government Code  
Section 7.9)

14

15 Joann Richmond  
Chief,  
Board Proceedings Division

16

17 For the Board of Susanne Buehler  
Equalization: Chief, Tax Policy Division,  
18 Sales and Use Tax Department19 Phil Bishop  
20 Business Tax Specialist III,  
Property and Special Taxes  
Department

21

22 Stephen Smith  
Staff Counsel IV  
Legal Department

23



24 ----oOo----

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5	Action Item 2	7
6	Speaker: Steven K. Alari	
7	SEIU Local 1000	8
8	Action Item 3	33
9	Speaker: Steven K. Alari	
10	SEIU Local 1000	34

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1 450 N STREET  
2 SACRAMENTO, CALIFORNIA  
3 JUNE 26, 2012  
4 ---oOo---  
5 ACTION ITEM 1  
6 ---oOo---  
7 MR. HORTON: Ms. Richmond, what is our next  
8 item?  
9 MS. RICHMOND: Our next item on today's agenda  
10 is the Business Taxes Committee. Ms. Yee is the Chair  
11 of that committee.  
12 Ms. Yee.  
13 MS. YEE: Thank you, Ms. Richmond.  
14 Uh, we have one item under the Business Taxes  
15 Committee, and that is proposed Regulation 4801 and  
16 amendments to Regulations 4601, 4603, 4604 and 4605

17 under the Cigarette and Tobacco Products Licensing Act.

18 We have one speaker on this item. Let me have  
19 him come forward and -- while the staff introduces the  
20 issue.

21 Good morning.

22 MS. BUEHLER: Good morning.

23 I am Susanne Buehler with the Sales and Use Tax  
24 Department. And with me today are Stephen Smith from  
25 our Legal Department and Phillip Bishop from the  
26 Property and Special Taxes Department.

27 We have one agenda item for your consideration  
28 this morning involving three action items affecting the

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1 Cigarette and Tobacco Products Licensing Act  
2 regulations. We will take each action item separately  
3 before moving to the next.

4 In Action Item 1 we ask that the Board approve  
5 and authorize for publication proposed amendments to  
6 Regulation 4601, Service of a Notice of Violation or  
7 Warning Notice, as agreed upon by staff and interested  
8 parties. Over the course of administering the  
9 provisions of a Licensing Act, staff has identified a  
10 number of notices requiring service.

11 The proposed amendments would provide a uniform  
12 service mechanism for all notices required under the

13       Licensing Act and its regulations.

14               We have one speaker today, after which we are  
15       happy to answer any questions you may have on this  
16       action item.

17               MS. YEE: Thank you, Ms. Buehler.

18               Uh, let me have the speaker introduce himself  
19       and --

20               MR. ALARI: Oh, sure.

21               Steven Alari, with SEIU Local 1000. I'm  
22       President of our Labor Council 782 and also a Senior  
23       Investigator at the Board. But I'm here on behalf of  
24       the SEIU Local 1000.

25               But Action Item Number 1, I don't have a  
26       comment on that one.

27               MS. YEE: Okay. All right.

28               MR. ALARI: Thank you.

5

1               MS. YEE: Um, can you just give me a sense of  
2       what item you're going to be speaking about?

3               MR. ALARI: Uh, Action Item Number 2, the  
4       transferring of the cigarette and tobacco products, and  
5       also Number 3, regarding the penalties.

6               MS. YEE: Okay. Very well. Thank you very  
7       much.

8               Uh, Members, discussion on, uh, Item Number 1?

9               Okay. Are we prepared to take action on that?

10 MR. HORTON: Move adoption of the staff  
11 recommendation.

12 MS. YEE: Okay.

13 Motion by Mr. Horton to adopt the staff  
14 recommendation. Second by Mr. Runner.

15 Without objection, that motion carries.

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1 ACTION ITEM 2

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3 MS. YEE: Okay. Ms. Buehler.

4 MS. BUEHLER: In Action Item 2 we ask that the

5 Board approve and authorize for publication either

6 staff's recommendation to publish proposed regulation  
7 4801, Transfers of Cigarette and Tobacco Products  
8 Between Retail Stores Owned by the Same Person. This  
9 regulation would provide for transfers of cigarettes and  
10 tobacco products between retail stores owned by the same  
11 legal entity that are supported by a transfer log or  
12 similar document and copies of invoices to be maintained  
13 at each location participating in the transfer.

14 Alternative 1 is embraced by the retailers of  
15 cigarette and tobacco products with multiple locations  
16 and formalizes the Board's current policies regarding  
17 documentation requirements for the transfer of  
18 cigarettes and tobacco products between retail stores  
19 owned by the same person.

20 Or, approve the California Distributor  
21 Association's and SEIU Local 1000's alternative. This  
22 alternative provides that any proposed regulations to  
23 prohibit the transfer of cigarette and tobacco products  
24 between any retail stores regardless of the ownership.  
25 Language was not submitted by the interested parties for  
26 this alternative.

27 And, again, we have one speaker, after which we  
28 are happy to answer any questions you may have.

7

1 MS. YEE: Okay. Thank you very much.

2 Mr. Alari --

3 MR. ALARI: Yes.

4 MS. YEE: -- on this item.

5 ---oOo---

6 STEVEN K. ALARI

7 ---oOo---

8 MR. ALARI: Well, thank you, Madam Chair and  
9 Members of the Board.

10 As I say, my name is Steven Alari. I'm  
11 speaking on behalf of Local 1000 and our President,  
12 Yvonne Walker, who had sent a letter which is included  
13 in your packet.

14 Uh, we represent the Business Tax, uh,  
15 Specialists, as well as Business Tax Compliance  
16 Specialists who are your investigators, inspectors out  
17 conducting the inspections out in the field, trying to  
18 combat the underground economy, as well as help  
19 administer the program of cigarette and tobacco, uh,  
20 products out there, and licensing, as well as making  
21 sure that people have their licenses, as well as that  
22 they've paid taxes on their cigarette and tobacco  
23 products.

24 We support -- we support Alternative Number 2  
25 and a bright line test, that it should not -- on behalf  
26 of the union, uh, supporting having a test where people  
27 cannot transfer cigarette and tobacco products.

28 The law, uh, AB 71 says that you -- uh,

1     retailer must buy from a licensed distributor/wholesaler  
2     and have that invoice. On those invoices, it has the  
3     retailer's cigarette and tobacco license number, retail  
4     license number, as well as their information and what  
5     the products they purchased.

6             By allowing the transferring of product --  
7     we've seen this confusion. I know the Board put out the  
8     new Publication 78 which kind of explained to people  
9     this transferring process. But our inspectors and  
10    investigators -- all across the state there's confusion  
11    about being able to do this.

12            First, when we adopted the law, it was clear we  
13    weren't allowing transfers. And then when the Board put  
14    out guidance that people could transfer, there were a  
15    lot of folks -- and we've had a lot of seizures where  
16    people, "Oh, I didn't know there was transfer  
17    regulations," or -- or they try to create the transfer  
18    document as you're -- they're traveling from one store  
19    to the other store to bring it to you, to try to, uh --  
20    there are those bad characters out there. There are  
21    good folks out there.

22            The big -- the big stores, the gas station  
23    chains, they don't transfer. They just buy it from  
24    their suppliers and keep it at their location. It's a  
25    lot of the little stores where we're finding the issues  
26    out there.

27            With a clear, bright line that you cannot  
28    transfer, it's real -- it would be much simpler and, uh,



1 we believe it would also, uh, provide more revenue to  
2 the state because there are those places where you have  
3 a couple stores where, uh, allows -- when you do  
4 transferring, it allows for blending. You could have an  
5 invoice for five boxes of Swisher Sweet, regular flavor,  
6 at store number one. You go to store number two and  
7 store number two says, "Oh, I have a transfer document  
8 here from store number one that we have, uh -- we  
9 bought -- transferred three boxes of Swisher Sweets."

10 Well, then we have to run over to store number  
11 one to make sure they don't have those, uh -- that  
12 product at the original store because, uh, you could do  
13 a transfer document and you slip in three boxes at the  
14 second location. You have paperwork, but it allows  
15 the con -- the opportunity for people to slip in untaxed  
16 tobacco products. And, as you know, the state loses  
17 \$90 million in un -- in untaxed tobacco products.

18 Now cigarettes have the tax stamp. That's --  
19 we know the tax has been paid. It's the tobacco  
20 products where there's issues out there.

21 And then, also, even like the transfer log and  
22 the information, the sample trans -- uh, excuse me,  
23 Exhibit Number 7 which is included in the packet,  
24 example on the first transfer it shows five boxes of

25 Romeo and Julieta cigars, 25 each. Well Romeo and  
 26 Julieta cigars, there's seven different product lines  
 27 under Romeo and Julieta; and under that, there's a total  
 28 of 44 different types of Romeo and Julieta cigars.

10

1 And, uh, it makes it very hard for the  
 2 inspectors and investigators to, uh, know that tax has  
 3 been paid on those products. Because you could have an  
 4 invoice for Romeo and Julieta cigars, but it could be  
 5 one of the 44 different types of cigars there.

6 Um, so we would encourage that you adopt  
 7 Alternative Number 2, making it real clear to the  
 8 taxpayers, they're just not transferring, and I believe  
 9 it would ensure better compliance out in the field.

10 Thank you very much.

11 MS. YEE: Thank you, Mr. Alari.

12 Uh, I know Ms. Steel has a question. But  
 13 before, um, I turn to her, uh, you raised a question  
 14 that I want to ask Mr. Smith. And that is, um, do we  
 15 have statutory authority to move in this direction?

16 MR. SMITH: I believe we do. There's no  
 17 express statutory authority for prohibiting transfers  
 18 between stores owned by the same person. There's also  
 19 no statutory authority that expressly allows such  
 20 transfers.

21 I think, um -- I think a regulation is

22 important because, as Mr. Alari said, there's confusion  
23 all over about what's going on here.

24 I think we are also only authorized to seize  
25 product when there is, uh, not evidence that tax was  
26 paid on the product. And staff believes that if these  
27 documentary -- if they followed the regulation, we would  
28 have adequate support to establish the tax was paid and

11

1 we're not authorized to, uh, seize product if it's,  
2 uh -- once tax has been paid on the product.

3 MS. YEE: Mm-hmm. Okay.

4 Uh, and then to the Department, is it true the  
5 large retailers don't transfer product?

6 MR. BISHOP: Well, that's, uh, not necessarily  
7 what I'm hearing from the large retailers. And, uh, I  
8 think we received, uh, support from Chevron which has a  
9 number of service stations throughout the state, and  
10 they sell cigarettes and tobacco products. And they  
11 were very supportive of the proposed regulation because  
12 they identified a number of instances that were  
13 business-friendly in terms of the need to transfer.

14 And one that was extremely important was if a  
15 store is abandoned, what do you do with the product? Do  
16 you leave it there, do you return it to the distributor,  
17 or do you move it to one of your other locations?

18           Um, so it -- it is occurring with the larger  
19 stores. Again, Chevron did provide support for it and I  
20 have received some phone calls -- they did not submit  
21 anything in writing, but -- from other large retailers  
22 that also encountered those similar positions or those  
23 situations when a store is abandoned or sold.

24           One of the other, um, situations -- and, again,  
25 it's identified in the issue paper -- is the vending  
26 machine operator. Vending machine operators, each  
27 vending machine location is a licensed location, and  
28 it's typically not owned by that particular retailer.

12

1   The location isn't, but the vending machine is. So, how  
2 do they take delivery at a vending machine?

3           I think the Licensing Act envisioned transfers,  
4 does not require that the item be delivered to the  
5 license location. It only says that the license -- that  
6 a license location -- uh, the license of a location be  
7 on the invoice.

8           Um, one instance is a cash-and-carry situation.  
9 If you are unable to transfer product, how would you do  
10 a cash-and-carry, say at a Costco or something like that  
11 where you're buying for multiple locations? You would  
12 have to buy, this is going to this location, this is  
13 going to another location. Typically this businessman  
14 is going to buy in bulk and move it to the various

15 locations.

16               So long as he's provided Costco with a licensed  
17 location, that he is a licensed retailer, Costco is,  
18 um -- has satisfied their invoicing requirements. And,  
19 um, that licensed retailer then is able to move that  
20 product to the location in which they plan on selling  
21 it, so long as they have evidence that tax was paid on  
22 it, which would be a copy of that invoice. And  
23 according to the reg., we also want to see a transfer  
24 log, to further document the sale.

25               MS. YEE: Okay, uh, thank you.

26               Uh, Ms. Steel, please.

27               MS. STEEL: You know, I like this proposed, uh,  
28 regulation because this is very much business-friendly

13

1 and flexibility for small stores. I'm not really  
2 concerned about big stores because small stores, you  
3 know, they cannot have big inventory there. Sometimes  
4 they are short. They can move, under same owner, to  
5 another store. I mean, you know, I just really want to  
6 go for that.

7               But having said that, those transfer documents,  
8 that what kind of -- are required by BOE? You know,  
9 what kind of things that they have to, um, document that  
10 when they transfer from one store to another?

11           MR. BISHOP: Well, it's identified in the  
12 regulation. It's the license location in which it was  
13 purchased under. So if -- um, so that would be the,  
14 like the receiving store, and then the license location  
15 of where it's being transferred to, and a full  
16 description of the product, um, and the invoice number  
17 and an invoice copy.

18           And to -- to Mr. Alari's comment regarding it's  
19 very difficult to specifically identify the product  
20 that's being transferred because they are so detailed  
21 and there are -- there are such a variety of products  
22 out there, that's true. But in looking at some of the  
23 invoices coming in from the distributors, um, those  
24 invoices have a description so you would -- you would,  
25 in essence, put the description that's on that  
26 invoice.

27           MS. STEEL: So as long as you have invoice  
28 there, then that description is right there --

14

1           MR. BISHOP: Correct.

2           MS. STEEL: -- that exactly what's been  
3 transferred.

4           MR. BISHOP: It should match what's on the  
5 shelf --

6           MS. STEEL: Okay. Thank you.

7           MR. BISHOP: -- what's being transferred.

3 MS. YEE: Okay. Mr. Runner, please.

9 MR. RUNNER: Uh, there's no doubt that -- that  
10 we've had confusion on this issue -- uh, on these issues  
11 coming before the Board. Um, and, uh -- and that it's  
12 an issue that -- that needs -- needs resolution.

13 Let me just ask, the concerns that have been  
14 brought up, uh, in regards to, uh -- you know, even  
15 with -- with transferred documentation, that somehow  
16 there could be this -- this difficulty in -- in escaping  
17 tax, do you believe that the regulations that are  
18 being -- being put in place, uh, along with the, uh, the  
19 required documentation's going to be there, uh, protects  
20 California taxpayers in regards to this issue, in  
21 regards to escaping tax?

22 MR. BISHOP: Well, we drafted this regulation  
23 in conjunction with the Investigations group and with  
24 their management. And their management is in on board  
25 with the proposal and the proposed reg. and has provided  
26 their input so that they can fully document and verify  
27 the tax paid status of the product.

28 And that is what the Licensing Act requires, is

15

1 that the tax -- that any retailer be able to prove that  
2 the tax was paid on that product. And we -- we believe,  
3 along with, uh, ID that, uh, this regulation satisfies;

4     that it does add a bit of a burden to the investigators,  
5     but, uh, from what we've been told, that's an absorbable  
6     cost.

7             MR. RUNNER: One of the concerns that I have --  
8     and I think, again, we need to bring clarity. There  
9     was -- there was certainly a lot of confusion which --  
10    which I think was difficult then for both the inspectors  
11    and then also for businesses out there. And so that's  
12    why I think this step is -- one of these two are  
13    important for us to bring in order to bring that  
14    clarity.

15            Uh, and I -- and I find myself supportive of  
16    the -- of the, uh, the action and recommendation by  
17    the -- by the Department at this point, uh, because I  
18    think the other side of this is -- is -- is even though  
19    I get the fact that there might be the additional  
20    follow-up work that might be a little more difficult for  
21    inspection at that point in the field, the fact is,  
22    these are still businesses out there, that I'm trying to  
23    figure out how it is that, again, if you've got product  
24    over in store A and you need this product over in store  
25    B, um, and you need to do it over the weekend because  
26    you just found out the inventory -- you know, you got to  
27    get inventory over there, to not have then that business  
28    have that inventory over in that store, uh, it seems to



1 be putting that business at a disadvantage.  
2 Particularly if you're a smaller business, where a large  
3 business can handle those issues or a larger -- again,  
4 some of the Chevron and when we talk about large, but  
5 I'm talking about even in that case, you've got  
6 individually owned franchises at that point that need to  
7 move product back and forth. Whereas, being the larger  
8 stores, the retailers -- the large retailer and whatnot  
9 may not have to worry about that. Some of those smaller  
10 retailers, even if they are part of a franchise chain at  
11 that point, may need to just be able to move -- have the  
12 flexibility of moving product about.

13 So, I guess my concern is that if the -- if the  
14 Department's secure enough, that we're able then to  
15 document that well enough for both the protection of the  
16 taxpayer and clear trails for the investigator, it seems  
17 to me we've gone a long ways to accomplish something  
18 that -- that will be beneficial.

19 MS. YEE: Thank you, Mr. Runner.

20 Mr. Horton.

21 MR. HORTON: Thank you, Madam Chair.

22 Um, you know, I share the investigator's  
23 concern about the commingling of the -- of the, uh,  
24 legitimate tax paid product with product that -- where  
25 there is no tax paid. And it's, uh, often done -- I  
26 mean, you'll find, even on the containers, when they  
27 bring in the containers, on the front end of the  
28 containers will be legitimate product that is properly

1 stamped and so forth, indicating all that. But on the  
2 back end is where all the fraudulent, uh, product is and  
3 the same thing happens.

4 But there is a concern that we need to address,  
5 and that's the concern of legitimate operators being  
6 able to, uh, make corrections in their inventory when  
7 that is necessary, be it as a result of an abandoned  
8 store, vending machine, the examples that you brought  
9 forth.

10 From an audit perspective, I do think that the  
11 regulation needs to put forth more internal controls,  
12 uh, as it relates to inventory control. I don't -- I  
13 haven't had a chance to review it again. But, uh, would  
14 like to have that opportunity, Madam Chair, and commit  
15 to review the regulation, work with the investigators  
16 and so forth.

17 Uh, my concern would be, when you transfer  
18 product in between stores, you do have that opportunity  
19 to commingle because part of the -- part of the -- the  
20 objective of the fraudulent activity is to produce a  
21 product that you cannot distinguish from the legitimate  
22 product. Uh, and even in some cases actually produce a  
23 tax stamp that you can place on it that looks the same.

24 And so, uh, therein is part of the challenge.  
25 And then you have the distribution or the ultimate sale  
26 of the product. And so the investigators are coming in

27 after the fact and trying to control this inventory.  
28 And you've got this, uh, self-serving document, for the

18

1 most part, identifying product being transferred, and  
2 you're auditing one store versus the other.

3 And -- and in some cases the stores may very  
4 well have different permits, so you may not even be  
5 auditing, unless the regulation specifically restricts  
6 the transfer between, uh, stores or locations that have  
7 the same, uh, permit.

8 MR. BISHOP: Same ownership.

9 MR. HORTON: Same owner -- well, same -- same  
10 permit preferably, but not necessarily ownership. There  
11 is a distinction often times.

12 Uh, but the concern would be commingling  
13 inventory. Are there any recommendations on how we can  
14 control that inventory? Uh --

15 MR. BISHOP: Well, I think, uh -- and I tried  
16 to address it in the issue paper itself, but I think,  
17 uh --

18 MR. HORTON: No, in -- in the regulation. Does  
19 the regulation address the concern about commingling  
20 inventory?

21 MR. BISHOP: And again --

22 MR. HORTON: Requiring -- one second.

23 MR. BISHIP: There's a --

24 MR. HORTON: I'm trying to help.

25 MR. BISHOP: Sure.

26 MR. HORTON: Requiring some form of inventory  
27 control, uh, so that you show the depletion of inventory  
28 on one side, increase of inventory on one side, total

19

1 inventory, we reconcile the -- the both -- the two  
2 and -- and we're able to make that verification.

3 MR. SMITH: I think the way the regulation  
4 language helps prevent blending is that the records have  
5 to be contemporaneous. They have to be in the store  
6 when we go in the store. They can't be produced after  
7 the fact.

8 And blending is undoubtedly a real problem.  
9 But blending can also occur even when there is not a  
10 transfer of inventory between stores.

11 Um --

12 MR. HORTON: I don't think the fact that  
13 they're contemporaneous -- that simply means that  
14 they're smart enough to do it in advance. Uh, that  
15 really doesn't address the challenge of commingling  
16 inventory.

17 It may be some inventory control requirements  
18 where you're required to, uh -- to maintain the  
19 inventory controls on both stores that reflects the

20     increase and decrease in inventory as it relates to this  
21     particular product. Uh, so that the front-line  
22     investigators can now have the -- the flow of  
23     information and the documents in order to reconcile the  
24     two.

25             Madam Chair, if I may --

26             MS. YEE: Yes.

27             MR. HORTON: -- uh, address the, uh -- the  
28     witness.

20

1             MS. YEE: Yes.

2             MR. HORTON: Uh, any thoughts in that regard?

3             MR. ALARI: Uh, I have to look at it more --  
4     uh, more closely, Mr. Chair -- or Mr. Chairman.

5             MR. HORTON: Okay.

6             MS. MANDEL: Member Yee?

7             MS. YEE: Yes. Ms. Mandel.

8             MS. MANDEL: Um, certainly what I'm hearing is  
9     a -- is a desire to study the regulatory language more  
10    closely. I think, um, what Mr. Smith was maybe  
11    referring to is that there is a reference to, um,  
12    keeping the logs and the invoices at both locations, um,  
13    which maybe goes a little bit --

14            MR. HORTON: Gets close.

15            MS. MANDEL: A little bit to what you were  
16    talking about.

17                   Um, but I -- and -- and the one thing that I  
18   heard, too, was whether the log, the sample log as  
19   reflected in the regulation -- because my understanding  
20   is the sample log is part --

21                   MR. BISHOP: It's actually just an -- an  
22   exhibit which will be, uh, like a document that we'll --  
23   that we'll identify on our website as an example.

24                   MS. MANDEL: Okay. But if the example is  
25   not -- if the specificity -- if the required specificity  
26   is not in the face of the sample log itself but is, by  
27   virtue of the attachment of the invoices, then you'd  
28   want them -- if -- if it went for -- if this went

21

1   forward, you'd want to make sure that the sample log was  
2   explicit enough, um, you know, because you don't -- you  
3   don't want to set up something where you're trying to  
4   be -- make sure that you have all the specific  
5   information in both locations so it can totally be  
6   tracked as best as it can with something that's  
7   unstamped, uh, and then find that you've created traps  
8   for the unwary retailer or, um, have created something  
9   where you're going to have retailers coming forward and  
10   saying I was somehow -- I was in substantial compliance  
11   with what you wanted and, you know, under general  
12   administrative practice for certain types of things --

13 and I don't know if it would apply here, but that  
14 that's, you know, sort of good enough.

15 So, if you're trying to really tie them down to  
16 exactitude, then you're going to have to go out and --  
17 and educate them about the exactitude that's required.

18 And when you mentioned the, um, larger  
19 retailers that have multiple locations, and there was a  
20 reference here about many of them might be franchises,  
21 what I saw in that e-mail was a reference to, um -- uh,  
22 if the BOE prohibits transfer from one legal entity to  
23 another, it will negatively impact us. And then here's  
24 a list of our retail operation concerns about transfers  
25 from store to store.

26 I thought that the way the regulation was  
27 drafted was you might have two loc -- two or more  
28 locations, business locations -- and of course our

22

1 licenses are all tied to a location -- but that all of  
2 those locations would be in the single ownership, single  
3 legal entity. And -- and your large operators, even if  
4 they're corporate-owned stores, they may have them all  
5 in separate legal entities for other purposes.

6 So, um -- and maybe even a little guy does, you  
7 know, I don't know. But maybe he's just renting space,  
8 so maybe he doesn't have the same kind of issues. But  
9 the restriction to single legal entity, because we want

10 to make sure it's really the same owner, they may be  
11 supportive because they think it covers them and it may  
12 in fact --

13 MR. HORTON: Not.

14 MS. MANDEL: -- not cover them.

15 So, again, that's another one where I'm not  
16 saying it should be broader if you do it. I'm just  
17 saying you might be -- it might -- with all these  
18 different issues, is it going to create -- everyone's  
19 going to have to know what -- absolutely, if it goes  
20 forward, how it really works and how it applies and that  
21 come to find out, oh, it doesn't apply to me, I did all  
22 these transfers or I closed a store and moved the  
23 inventory to another store. But because I have them in  
24 separate legal entities, even though I have beautiful  
25 documents, it's not going to work.

26 If you do it, people have to know how it really  
27 works and that they're going to lose the product  
28 otherwise or they need to send it back to the

23

1 distributor or something.

2 But that was the one thing -- disconnect I  
3 noticed between the e-mail that you had from the large,  
4 uh, company and the words that are in -- in the reg.  
5 And I don't know if you guys discussed that in



6 interested parties at all because a lot of this, um --  
 7 the attachments were prior to the last interest --  
 8 second interested parties meeting.

9 So, do you have a thought?

10 MR. BISHOP: I think when, um, the large  
 11 retailer Chevron that -- that chimed in, um, they  
 12 have -- obviously they have franchise locations, but  
 13 they also have corporate-owned locations. And they  
 14 were -- I believe they were talking about their  
 15 corporate-owned locations.

16 So, I -- and I also believe that the regulation  
 17 is fairly clear that it states that it has to be the  
 18 same -- the same legal entity must, um, own both  
 19 locations. Let's just talk about two as an example.  
 20 And then it further goes on to state that, you know,  
 21 sales between locations are bought, you know, between  
 22 non-owned retailers are in --

23 MR. HORTON: Illegal.

24 MR. BISHOP: There's a statute that prevents  
 25 that, that is --

26 MS. MANDEL: Right.

27 MR. BISHOP: And so --

28 MS. MANDEL: Right. I just -- the large

24

1 retailer, he may have corporate-owned locations, but  
 2 they're corporate-owned because, you know, the big

3 corporation at the top, they're corporate-owned. I  
4 don't know -- you know, I don't know their business. I  
5 don't know --

6 MR. BISHOP: Right.

7 MS. MANDEL: -- if every single one of their  
8 corporate-owned locations is technically in the same  
9 legal entity or not. And, um, you know, with the  
10 different types of liabilities that might come to pass  
11 at -- at a, um, gasoline station, I might suspect that  
12 they're not.

13 But that's their problem, not my problem, how  
14 they own their stuff. But if they, uh -- so you're  
15 saying if they actually had them in separate corporate  
16 subsidiaries, that's not the same legal entity for our  
17 purposes.

18 MR. BISHOP: Correct.

19 MS. MANDEL: Okay.

20 MS. YEE: Mr. Horton.

21 MR. HORTON: Yeah, I would agree with  
22 Ms. Mandel in that regard. I think we may need just a  
23 tad bit of clarification, um, as it relates to defining,  
24 uh, legal ownership. Certainly there are a number of  
25 other bodies of law that describe it differently, and  
26 where you could actually have a holding company that is  
27 the legal ownership of all the different entities.

28 So when you're -- but based on my experience

1 in -- in dealing with this as the author of the  
2 legislation, as well as dealing with it as a Member of  
3 the Board, the larger corporations, they sort of get it.  
4 Uh, and they certainly need to be able to transfer the  
5 product; that is a challenge.

6 But, uh, we have to be able to control the  
7 illegal activity as well, the underground activity. And  
8 I think the requirements that, uh -- that will address  
9 that wouldn't be a burden on the larger companies and  
10 shouldn't be a burden on the smaller companies. Most of  
11 them will be required by GAAP, the Generally Accepted  
12 Accounting Principles and certain levels of -- there  
13 needs to be certain, uh -- uh, levels of inventory  
14 control. Irrespective of what the regulation says, it's  
15 just inherent in the business practice.

16 So to require that, shouldn't be that, uh, much  
17 of a burden on even the smaller taxpayer because  
18 arguably they would want to control the inventory so  
19 that they're able to treat each location as a separate  
20 call center, as well as manage -- manage their -- uh,  
21 their needs, uh, as far as the demands that are placed  
22 on the marketing, purchasing, and so forth.

23 So, we might want to take a look at that and  
24 engage the investigators directly. I appreciate the --  
25 the participation of management and the participation of  
26 staff as well. But often times the individuals in the  
27 warehouse can tell you how to move the product just a  
28 little bit better or how to protect the product just a

1     little bit better.

2             And, uh, Madam Chair, if it's okay with the  
3     Members, I will commence, spend a little time in -- in  
4     that process.

5             MS. YEE:   Okay.

6             Uh, Mr. Alari, any thoughts?

7             MR. ALARI:  Yeah, I just wanted to add one more  
8     point.

9             On Section (D) of the proposal, I think it's a  
10    really good language about that, uh, if they try to  
11    create the log after the seizure or citation, that we're  
12    not going to accept them.  And they can't be used for  
13    return of the seized product.

14            One thing that if you do really look at it or  
15    for future regulation changes, you might want to  
16    consider if they create the, uh -- create during the  
17    inspection or provide it after the seizure, because  
18    we've had people who -- from our investigators have  
19    dealt with people who are trying to create the log while  
20    you're there or, uh -- or on their way to the location.

21            So that would be helpful; if they don't have  
22    the log prior to you coming in to do your inspection,  
23    then we won't accept it.  But just something to look at  
24    if we relook at this issue in the future.

25            But it's a very good language now, but if we

26 could make it a little better, we'd suggest.

27 MS. YEE: Okay.

28 MR. ALARI: Thank you.

27

1 MS. YEE: Further discussion, Members, on this  
2 particular action item?

3 Okay. It appears that, um, there is interest  
4 in deferring this, uh, to allow staff to work with  
5 Investigations further on refining the language and, uh,  
6 taking into consideration some of the concerns Mr. Alari  
7 has expressed. But I think we can do that by tightening  
8 up some of the -- the language in the -- in the reg.

9 Mr. Runner.

10 MR. RUNNER: Just procedurally, uh, as that  
11 discussion goes on, how do we -- since this went through  
12 an interested parties meeting --

13 MS. YEE: Mm-hmm.

14 MR. RUNNER: Or -- or discussion, how do we --  
15 do we actually -- I mean, do -- do they end up coming  
16 back and seeing then whatever the product is that comes  
17 out of these next level of discussions? Or, just  
18 procedurally, just wondering how that works since this  
19 grew out of an interested parties to which all these  
20 people were a part of.

21 MS. YEE: Mm-hmm. Mm-hmm. Yeah.

22 MR. RUNNER: And now we're saying, "Okay, we  
23 want to go back and talk to some more."

24 MS. YEE: Yeah. I think staff will -- well,  
25 you can describe the process.

26 MR. RUNNER: Okay.

27 MS. YEE: But, um, they'll confer with  
28 Investigations. Any, uh, recommended changes will then

28

1 be drafted, circulated again for comment.

2 MR. RUNNER: Okay.

3 MS. BUEHLER: Right.

4 MR. RUNNER: That's all. That's -- thank you.

5 MS. YEE: Yeah. Okay.

6 Uh, Ms. Mandel.

7 MS. MANDEL: Uh, I was just wondering about  
8 timing.

9 MS. YEE: Yeah. Um, let's see, we are in June.  
10 Possibility of bringing this back by August?

11 MR. BISHOP: Uh, this particular regulation,  
12 that would require -- were you thinking an interested  
13 parties meeting?

14 MS. YEE: No -- well, no. Back to the Board.  
15 I don't know -- I mean, this -- the issues are discrete.  
16 I think it's really looking at the proposed language  
17 and, uh, the Department conferring with Investigations  
18 with respect to how to tighten up some of the provisions

19 in the discussion today.

20 MR. BISHOP: Yeah. I'm a little -- I'm not  
21 really clear on how to shore up an inventory situation  
22 either, um, in a regulation.

23 MS. YEE: I'm sorry, repeat that.

24 MR. BISHOP: In terms of a -- what -- what  
25 Mr. Horton was suggesting regarding inventory  
26 controls --

27 MS. YEE: Mm-hmm.

28 MR. BISHOP: -- I'm not necessarily sure how to

29

1 get that into a regulation form. Um, I just don't know  
2 how that would -- how that would play out.

3 MR. HORTON: If I may, Madam Chair.

4 MS. YEE: Yes, Mr. Horton.

5 MR. HORTON: Um, it may not be just in the  
6 reg -- in the regulation. We may have to address this  
7 in the audit manual. Um, but certainly there is a way  
8 to do it.

9 In the construction industry the auditors are  
10 required to do a, um -- a cost accountability test in  
11 order to identify. And the situation is similar because  
12 you have short ends and you have other product that's  
13 not necessarily sold or not necessarily consumed on  
14 the -- and so they have to go in and do a cost

15     accountability test. And therein there are certain  
16     inventory documents that are required to be available.  
17     And if they're not available, then of course the measure  
18     of tax is -- ends up being higher than what it really  
19     may be.

20             So there are plenty of examples on how to  
21     accomplish this objective, and I'd be more than willing  
22     to share those with you given a little more time.

23             MR. BISHOP: So those go on the -- on the audit  
24     side, not so much on the inspection side? Because I  
25     don't think inspectors actually do audits when they're  
26     out there, they just look at what's on the shelf and --  
27     and --

28             MR. HORTON: No, what I'm sharing is that there

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1     are examples within the audit manual. And of course the  
2     audit manual does govern the actions of the investigator  
3     as well, uh, when they're conducting their  
4     investigations and coming up with this.

5             So, um, I'm just, uh -- although, I -- Madam  
6     Chair, I don't necessarily think this is the venue in  
7     which to solve this problem, but I do, uh, differ with  
8     staff's, uh, opinion that they can't solve it.

9             MS. YEE: Yeah.

10            MR. HORTON: I believe they can, and I believe  
11     they have the fortitude, the ability, and intellectual



12 capacity to address this and come up with a solution.

13 MS. YEE: Uh, I would agree. And let me just  
14 say, I'm happy, as Chair of the committee, to continue  
15 working with the staff. But I think the direction here  
16 is to have, um, certainly further consultation with the  
17 Investigations Division, uh, on the issues that we've  
18 raised today, looking at tightening up the provisions  
19 that were of concern to the Members. And, uh, I think  
20 we utilize, uh, further tools with respect to the either  
21 the audit manual or office memos to really, um, provide  
22 further clarification.

23 I would agree, a lot of this probably doesn't  
24 belong in a reg., but, uh, just to be clear with respect  
25 to what the expectation is, okay.

26 Um, let's go ahead and do that. I would like  
27 to see an accelerated process. Um, and if we can get  
28 this back by August, terrific. If not, let's stay in

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1 close contact and see what works. Okay.

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1 ACTION ITEM 3

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3 MS. YEE: Uh, while everybody's convened, I'd

4     like to just take up the penalty issue, uh, if there's  
5     any public comment on that as well.

6             Uh, Ms. Buehler, do you want to introduce that?

7             MS. BUEHLER: Certainly. In Action Item 3, we  
8     ask that the Board approve and authorize for publication  
9     either staff's recommendation to amend Regulation 4603,  
10    Penalties for Licensed or Unlicensed Retailers;  
11    Regulation 4604, Penalties for Licensed or Unlicensed  
12    Wholesalers and Distributors; and Regulation 4605,  
13    Penalties for Licensed or Unlicensed Manufacturers and  
14    Importers.

15            This recommendation provides staff with a  
16    five-day suspension period in addition to the current  
17    zero-day, 10-day and 20-day suspension periods that may  
18    be imposed when mitigating circumstances are present,  
19    including the recommended technical corrections.

20            Or, staff's alternate proposed amendments to  
21    the regulations as recommended at the first interested  
22    parties meeting, provide staff with a range of  
23    suspension periods between zero days and 20 days that  
24    may be imposed when mitigating circumstances are  
25    present, including the recommended technical  
26    corrections.

27            Although staff is no longer recommending  
28    adoption of these amendments, the alternative language

1 is being provided for your consideration.

2 Again, we have one speaker, after which we are  
3 happy to answer any questions you may have.

4 MS. YEE: Okay. Thank you, Ms. Buehler.

5 Mr. Alari.

6 ---oOo---

7 STEVEN K. ALARI

8 ---oOo---

9 MR. ALARI: Yes, Steven Alari, representing  
10 SEIU Local 1000.

11 In our letter, our President's letter to you,  
12 Yvonne Walker's letter, it said it's very important that  
13 we have a deterrent for those who wish to violate the  
14 law. And we supported, uh, in keeping the current  
15 regulation.

16 But looking at the two alternatives, uh, we  
17 would support Alternative 1 versus Alternative 2 because  
18 our -- our members are the ones who are required to go  
19 out and do the undercover buy to see if the people are  
20 following the suspension or -- and not selling during  
21 those periods. And to have zero to 20, you know 1, 2,  
22 3, 4 days, that would be hard.

23 My territ -- the members who I represent in --  
24 up this area, we have 19 counties. And to be able to  
25 get up to Modoc County or Siskiyou County, with one  
26 two-day suspension would be unreasonable, we believe, on  
27 behalf of our members to be able to do a hundred percent  
28 inspections. And we believe five days minimum is -- is

1 much better than having zero to 20.

2 MS. YEE: Okay.

3 MR. ALARI: Thank you.

4 MS. YEE: Thank you.

5 Discussion, Members?

6 Ms. Steel.

7 MS. STEEL: You know, um, when staff came up  
8 with five days and I was really happy about it because  
9 it was taxpayers friendly. But I was thinking about it  
10 that after an inspection, that actually 44 percent of  
11 the taxpayers getting zero suspension days, um, but  
12 still it's violation. But after we put five days, I am  
13 concerned those 44 percent might get, instead of zero  
14 days, it's going to be five days now because five days  
15 less than 10 days. So how we going to, uh, practice  
16 this after -- if we vote this today?

17 MR. BISHOP: Well, staff currently has, as  
18 you -- as you noted, the 10- and the 20-day and the zero  
19 day --

20 MS. STEEL: Right.

21 MR. BISHOP: -- when there's mitigating  
22 circumstances. Um, there's two levels of appeal, and  
23 most of the suspension periods are reduced at that first  
24 level.

25 MS. STEEL: Right.

26 MR. BISHOP: Which is when staff -- program

27 staff is actually, um, handling the appeal.

28 Two things can occur. There -- there may be

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1 some of the zero days that would rise to the level of a  
2 five-day and -- but there may be some of the 10-day  
3 suspensions that will drop to the level of a five-day.  
4 And so it's hard to say if there will be more as a  
5 result of it or if it's going to be fairly constant  
6 figure. Um --

7 MS. STEEL: So, my question is, so 10 days to  
8 five -- reduced to five days we might going to have  
9 more? Or the staff are going to be much tougher now, so  
10 zero days to five days they getting, it's going to be  
11 much more. That's what I'm asking.

12 MR. BISHOP: Yeah. I don't believe staff's  
13 going to be --

14 MS. STEEL: Bottom line is, that's what I'm  
15 really concerned about.

16 MR. BISHOP: -- more tough in terms of -- I  
17 think they're going to evaluate each case on its own  
18 merits. And today there's -- you know, they look at  
19 volume of the, uh -- of sales versus the amount that's  
20 being seized. If there's been prior inspections that  
21 did not result in any sort of, uh, seizure, they look  
22 at, um -- if there has been prior violations, they look  
23 to, you know, how -- how new the -- is it -- is it a new

24 operation? Um, because that individual may not have  
25 invoices for everything on the shelf.

26 MS. STEEL: Okay.

27 MR. BISHOP: And it's sort of a -- and they --  
28 they do what they call a peer review within their group,

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1 um, so that they're consistent with their treatment.  
2 And there -- there could be some more lenience. Um, I  
3 don't -- in all honesty, I don't think we're going to  
4 see an increase. They'll exercise their judgment on  
5 these cases. But, uh, five days -- I think in many  
6 cases five days will replace the 10-day suspension  
7 period.

8 MS. STEEL: Okay.

9 MR. BISHOP: And, uh --

10 MS. STEEL: So there's -- you're looking at the  
11 inventory and then how much violation they have. So  
12 your staff are going -- going to go out there and they  
13 going to do the same practice.

14 MR. BISHOP: Yes.

15 MS. STEEL: So a lot of times you think that 10  
16 days were too tough, and then it can be five days. But  
17 those zero days, the first violation, that that's going  
18 to be staying as is.

19 MR. BISHOP: I think -- uh, well, I think there

20 will be some zero days --

21 MS. STEEL: Some, but --

22 MR. BISHOP: -- that will rise to five.

23 MS. STEEL: Okay.

24 MR. BISHOP: And looking at the sheer numbers,

25 um, it may be one or two a month additional.

26 MS. STEEL: Okay. Thank you.

27 MR. BISHOP: I mean that was the guess

28 anyway.

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1 MS. YEE: Okay. Thank you, Ms. Steel.

2 Mr. Runner.

3 MR. RUNNER: Just remind me, what was -- what

4 was -- what was the problem we were wanting to solve

5 here?

6 MR. BISHOP: The problem was 10 days was -- was

7 a rather harsh penalty.

8 MR. RUNNER: Okay.

9 MR. BISHOP: And there's occasions when it --

10 10 is almost two weeks of being shut down.

11 MR. RUNNER: Mm-hmm.

12 MR. BISHOP: And so -- but it --

13 MR. RUNNER: But yet it rose to --

14 MR. BISHOP: -- will require --

15 MR. RUNNER: But it rose to more than zero.

16 MR. BISHOP: But it rose to more than zero, and



17 they needed some sort of deterrent. So staff would like  
18 to have the five days with which to have that middle  
19 ground on.

20 MR. RUNNER: Mm-hmm.

21 MR. BISHOP: Um, and again, getting back to  
22 Ms. Steel's -- about the numbers. It's hard to say if  
23 there will be more, um, suspensions of a five-day versus  
24 a zero as a result -- well, not of a zero, but zeros  
25 that will increase the number of --

26 MR. RUNNER: Mm-hmm.

27 MR. BISHOP: -- suspension periods. Um, but  
28 granted some of the 10 will be --

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1 MR. RUNNER: Right.

2 MR. BISHOP: -- will come down to five, so it  
3 could be a wash.

4 MR. RUNNER: So in terms of adding then the  
5 five-day, was there -- what was the industry's concern  
6 out there? Or was there a concern?

7 MR. BISHOP: I think it was staff's -- it was  
8 more staff's concern with the harshness of the 10-day  
9 penalty. And they needed to put -- or 10-day  
10 suspension. And they needed a suspension period because  
11 the violation may have been the second violation, so  
12 they had to go to some step, even though it was a small,

13 um -- small dollar amount that was seized, it may have  
14 been the second, uh --

15 MR. RUNNER: Okay.

16 MR. BISHOP: -- instance.

17 MR. RUNNER: So I guess, what I think I heard  
18 you say is that certainly there will be some of those  
19 zeros that may go to five. But there certainly could  
20 have been some of those tens that end up going back to  
21 five then, too.

22 MR. BISHOP: Right.

23 MR. RUNNER: In terms of an array of choices.

24 MR. BISHOP: Right.

25 MR. RUNNER: Okay. Thank you.

26 MS. YEE: Thank you, Mr. Runner.

27 Ms. Steel.

28 MS. STEEL: I have one more question.

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1 MS. YEE: Yes.

2 MS. STEEL: You know, the suspension always  
3 starts from Friday, so that's going to hurt business on  
4 Friday and weekend businesses.

5 Is there any way possible we can change the  
6 program that suspension starts on Monday? I mean little  
7 thing helps for the taxpayers here.

8 MR. HORTON: That could increase the time or  
9 decrease the time.

10 MS. STEEL: No, it's not. But --  
 11 MR. BISHOP: Well, it --  
 12 MS. STEEL: It's five days, it stays five days.  
 13 MR. BISHOP: Currently it's, uh -- it's  
 14 system-generated. But that can be looked at and  
 15 modified.  
 16 MS. MANDEL: What do you mean system-gen --  
 17 MR. BISHOP: Well, the notice is --  
 18 MS. MANDEL: I mean, is it always Friday --  
 19 MS. STEEL: It always starts Friday.  
 20 MS. MANDEL: -- the way she says?  
 21 MS. STEEL: Mm-hmm.  
 22 MR. BISHOP: Yes, when there's been an appeal.  
 23 And reason being, on Wednesday's the batch. They batch  
 24 all of these various, uh, notices that are going to go  
 25 out. Thursday they're reviewed to make sure that, uh,  
 26 they're correct. And Friday they're mailed. And then  
 27 two weeks out from that is the setting of the suspension  
 28 period. So that occurs on a Friday.

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1 And so, to change the batch processing, um,  
 2 it's --  
 3 MS. STEEL: You don't have to change batch  
 4 processing itself, but, you know, you can just give them  
 5 couple more days so it can start -- instead of two

6 weeks, you can do two weeks plus two days. I mean --

7 MR. HORTON: What?

8 MR. BISHOP: Yeah. I mean, IRIS actually

9 enters the dates --

10 MS. STEEL: Yeah.

11 MS. YEE: Yeah.

12 MR. BISHOP: -- based on that. So it's

13 hard-coded. It can be changed.

14 MS. STEEL: Thank you.

15 MS. MANDEL: Can I ask a follow-up?

16 MS. STEEL: I want that to be changed.

17 MS. YEE: Yes.

18 Ms. Mandel.

19 MS. MANDEL: Um, with respect to the five days,

20 um, is the suspension period of business, open days for

21 the business, or is it just calendar days?

22 MR. BISHOP: It's, um, five calendar days, and

23 it's only for cigarette and tobacco products, so the --

24 MS. MANDEL: Right. No, I understand that.

25 Okay. Um, do -- are our guys working weekends?

26 MR. BISHOP: I don't think so.

27 MS. STEEL: No, most stores open.

28 MS. MANDEL: No, I understand that. But with

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1 a -- with a five-day -- with a five-day suspension and

2 you're telling me they're always starting on Friday,

3     um --

4             MR. BISHOP:  So Monday or Tuesday would be  
5     their opportune days for inspection.

6             MS. MANDEL:  So, I think that sort of just adds  
7     to the when -- when do inspections --

8             MR. RUNNER:  Or three days.

9             MS. MANDEL:  -- start a little bit if we're --  
10    when we're going -- if we're going to have the five days  
11    because -- I mean, I -- maybe it doesn't impact our  
12    guy's ability to get in.

13            At first I was -- didn't realize there was this  
14    Friday thing and I was, uh, a little concerned about  
15    something like Thanksgiving where you'd have four days  
16    in a row where our guys aren't on the street, you know,  
17    doing inspections.  But that only happens once a year  
18    where we have four days in a row.  Um, the most we ever  
19    usually have, I guess, would be three with a Monday  
20    holiday.

21            But in terms of implementation, if you get the  
22    five days, that might fit, to give the inspectors the  
23    most ability to get back in during -- I mean, you know,  
24    I'm not a -- I'm the administrative side, but it just --

25            MS. YEE:  Yeah.

26            MS. MANDEL:  -- sort of strikes me that if it's  
27    always going on Friday and everyone knows our guys  
28    aren't out on the weekend --

1 MS. YEE: Right.

2 Mr. Alari.

3 MS. MANDEL: -- or on a holiday --

4 MR. RUNNER: It gives you two free days,

5 doesn't it?

6 MS. MANDEL: Yeah.

7 MR. ALARI: Well, our -- our members do work on

8 weekends --

9 MS. YEE: Okay.

10 MR. ALARI: -- when needed, and, uh -- and

11 we'll adjust our schedule if necessary.

12 MS. YEE: Okay.

13 MR. ALARI: But the Friday was an issue that

14 our members did raise; if it's a five-day, then it would

15 be tough.

16 MS. YEE: Mr. Alari, restate your position on

17 this. What's your position?

18 MR. ALARI: Oh, our position is we support --

19 between the two options, we would support the

20 five-day.

21 MR. RUNNER: You just didn't like the zero

22 through 20 one or something, right?

23 MR. ALARI: Oh, I think zero -- the 20, 10 and

24 zero, we supported that.

25 MS. YEE: Yeah.

26 MR. ALARI: And that was the letter that came

27 to you --

28 MR. RUNNER: Okay.

1 MR. ALARI: -- from our President.

2 MS. YEE: Mm-hmm.

3 MR. ALARI: Of the two alternatives before the  
4 Board, we would prefer the -- the five-day --

5 MS. YEE: -- five-day.

6 MR. ALARI: -- minimum.

7 MS. YEE: Okay. All right. Very well. Thank  
8 you.

9 Further discussion, Members, on the penalty  
10 amendments?

11 Okay. Uh, motion?

12 MR. RUNNER: I would move the staff  
13 recommendation. However, I would like us to look at the  
14 issue in regards to the starting dates, particularly on  
15 the five-day.

16 MR. BISHOP: And -- and what would be the  
17 preference in terms of starting date?

18 MS. STEEL: Monday.

19 MR. RUNNER: Well --

20 MR. BISHOP: A Monday, if it's not a holiday?

21 MS. STEEL: Any day other than Friday --

22 MS. YEE: -- Friday.

23 MS. YEE: -- and Saturday.

24 MR. RUNNER: Yeah.

25 MS. YEE: Yeah, okay.

26                   Um, motion by Mr. Runner, uh, to adopt the  
27   staff recommendation with the suggested amendment of,  
28   uh, revising the starting day. Uh --

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1                   MR. HORTON: Second.  
2                   MS. YEE: Second by Mr. Horton.  
3                   Objection?  
4                   Hearing none, okay, such will be the order.  
5                   Thank you. So we'll see that coming back to us  
6   as well.  
7                   Okay. Mr. Alari, thank you.  
8                   MR. ALARI: Thank you.  
9                   MR. RUNNER: Thank you.  
10                  MS. YEE: Okay. Um, that concludes the  
11   Business Taxes Committee. It is adjourned. Thank you  
12   very much.

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I, KATHLEEN SKIDGEL, Hearing Reporter for the  
California State Board of Equalization certify that on  
June 26, 2012 I recorded verbatim, in shorthand, to the  
best of my ability, the proceedings in the  
above-entitled hearing; that I transcribed the shorthand  
writing into typewriting; and that the preceding pages 1  
through 45 constitute a complete and accurate  
transcription of the shorthand writing.

Dated: July 11, 2012

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KATHLEEN SKIDGEL, CSR #9039

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Hearing Reporter

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**BOARD OF EQUALIZATION****BUSINESS TAXES COMMITTEE MEETING MINUTES**

HONORABLE BETTY T. YEE, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

MEETING DATE: JANUARY 15, 2013, TIME: 10:00 A.M.

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**ACTION ITEMS & STATUS REPORT ITEMS****Agenda Item No: 1****Title:** *Proposed Regulation 4801, Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person.***Action 1****Proposed Regulation 4801, Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person.****Issue:**

Request approval and authorization to publish staff's proposed Regulation 4801 formalizing the current policy on transfers of cigarettes and tobacco products between retail stores owned by the same person; or direct staff to draft a proposed regulation that prohibits the transfer of cigarettes and tobacco products between any retail stores regardless of the ownership.

**Committee Discussion:**

Staff introduced the topic for discussion. Mr. Steven Alari, representing SEIU Local 1000, explained that SEIU has removed their previous concerns after additional language to the regulation was added requiring that the transfer logs must be provided to ID staff at the start of the inspection and further stipulate that transfer logs provided during or after the inspection will not be accepted. Mr. Dennis Loper, representing California Distributors Association, opposed staff's proposed Regulation 4801, stating this proposal would make it easier for a retailer to blend un-taxed tobacco products with tax-paid tobacco products and therefore increase evasion, and expressed support for alternative two, which prohibits transfers between any retail stores regardless of the ownership.

Mr. Runner expressed concern with the "no-transfer" alternative because it would require small business owners to maintain a larger inventory at each location to compensate for not allowing transfers and was supportive of staff's proposed regulation.

Mr. Horton noted that there are limited instances where a retailer may need to transfer incidental amounts of cigarettes and tobacco products, but that bulk transfers should be handled by licensed distributors or wholesalers. Mr. Horton expressed his concern that staff's proposed regulation does not limit the amount of cigarette or tobacco products transferred and may make it easier to evade the taxes. Mr. Horton suggested that staff add a requirement to the proposed regulation that would allow only small incidental transfers and continue to maintain the recommended inventory controls in the regulation.

Mr. Loper stated that he opposes any transfers but if transfers are allowed, they should be limited to emergency situations and should only be allowed upon notification to the Board. Mr. Runner stated he would support a limit or cap because he did not envision unlimited transfers but would not support requiring the retailer to contact the Board each time they transfer product.

After a general discussion, the matter was deferred so staff could reformulate the regulation in order to address limiting transfers and reach out to interested parties to discuss the impact of limiting transfers and to determine a reasonable transfer limit. Additionally, Ms. Mandel noted that since the matter would be deferred, staff should further clarify the term “legal entity” in referring to a natural person.

### **Committee Direction:**

The Board directed staff to conduct outreach with interested parties to convey the Board’s desire to limit transfers and to determine a reasonable limit. Ms. Yee noted that she would work with staff on a timeframe.

## **Action 2**

**Authorize Publication of Amendments Approved at the June 26, 2012, BTC Meeting to Regulations 4601, *Service of a Notice of Violation or Warning Notice*; 4603, *Penalties for Licensed or Unlicensed Retailers*; 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*.**

### **Issue:**

Request approval to publish amendments approved at the June 26, 2012, BTC Meeting to Regulations 4601, *Service of a Notice of Violation or Warning Notice*; 4603, *Penalties for Licensed or Unlicensed Retailers*; 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*.

### **Committee Discussion:**

There was no discussion of this item.

### **Committee Action:**

Upon motion by Mr. Horton and seconded by Ms. Steel with direction to staff to come back in a year with a report on staff’s use of the five-day suspension period included in the amendments to Regulations 4603, 4604 and 4605, without objection, the Committee approved for publication the proposed regulatory amendments. A copy of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 are attached.

**Agenda Item No: 2****Title: Proposed amendments to Regulation 1685.5, *Calculation of Estimated Use Tax – Use Tax Table.*****Issue:**

Request approval and authorization to publish proposed amendments to account for the new registration requirements imposed on certain retailers.

**Committee Discussion:**

Staff introduced the issue for discussion and explained that the proposed amendments would apply to the 2013 use tax table, which covers purchases made during the 2013 calendar year. Staff also noted that based on data from the Franchise Tax Board (FTB), the number of taxpayers reporting on the use tax line of their FTB returns nearly doubled from 2011 to 2012 with a revenue increase of \$9.8 million. Ms. Gina Rodriguez, representing the California Taxpayers Association, stated that taxpayers were well served by the interested parties' process and staff was responsive to their concerns. Ms. Rodriguez concluded by expressing support for staff's recommendation.

**Committee Action:**

Upon motion by Mr. Horton, seconded by Ms. Mandel, without objection, the Committee approved and authorized for publication the proposed amendments. A copy of the proposed amendments to Regulation 1685.5 is attached.

**Agenda Item No: 3****Title: Regulation 1502, *Computers, Programs, and Data Processing*, and Regulation 1507, *Technology Transfer Agreements*.****Issue:**

Whether to amend Regulation 1502, *Computers, Programs, and Data Processing*, to clarify how sales and use tax applies to transfers of prewritten software recorded on tangible storage media; and/or amend Regulation 1507, *Technology Transfer Agreements*, to clarify how the technology-transfer-agreement statutes apply to transfers of prewritten software recorded on tangible storage media.

**Committee Discussion:**

Staff introduced the topic for discussion. Staff explained that, if staff's recommendation is approved, it anticipates holding one interested parties meeting in March to discuss the application of tax to optional software maintenance contracts that include the transfer of a back-up copy of the same or similar prewritten software recorded on tangible storage media and two interested parties meetings, one in April and one in June, to discuss the application of tax to site license transactions. Staff further stated that they would present both issues to the Board at the August Board meeting.

Mr. Julian Decyk from Paul Hastings LLP clarified that their written submissions did not make specific recommendations to amend Regulation 1507, as indicated in the formal issue paper, and

their purpose was to base the discussion for potential amendments on their understanding of an accurate statement of the facts and law to avoid potential for an invalid regulation. Mr. Decyk also questioned the need for a regulation to implement the statutes. Mr. Decyk also argued that staff's discussion papers failed to substantially respond to asserted factual corrections and legal analysis which he previously presented to staff.

Mr. Mark Nebergall, representing the Software Finance and Tax Executives Council and a broad-based coalition of companies and trade associations (e.g., Silicon Valley Leadership Group), expressed general support for staff's recommendation. Mr. Nebergall also requested the Board consider the proposal to use a percentage split approach, with respect to software sold on TPP other than a separate tangible storage medium (i.e., what staff generally refers to as "embedded software"), to develop a regulation that allows companies to sell products with a clear understanding of their sales and use tax responsibilities.

Ms. Gina Rodriguez, representing the California Taxpayers Association, stated that if there is a need for regulatory amendments, they would like to continue to work with staff on proposed language which considers the needs of the software industry, as well as other industries.

Ms. Yee commented on the need to adopt proposals that are on a solid legal foundation, and clarity is of the utmost importance with respect to implementation, administration, and compliance and audit requirements.

Mr. Horton requested that staff address whether there is a need for a regulation or not. Staff noted that we currently have Regulation 1502 which addresses computer programs and Regulation 1507 that pertains to technology transfer agreements. Staff explained that to the extent that we would further define technology transfer agreements, staff thought it would be most appropriate to incorporate the amendments to Regulation 1507. Staff also explained that if we were to treat computer programs in a manner that is different than other property, staff believes it would be most appropriate to incorporate those amendments in Regulation 1502. Staff further stated that it remains open to further discussion as to the best method of amending either of the regulations.

Mr. Horton expressed the need for clarification and guidance to industry and audit staff and explained that this has historically been codified through the regulatory process rather than the audit manual alone for the purpose of providing guidance to all affected parties.

Lastly, staff initiated a corrective comment regarding the fact that the issue paper misconstrued Ernst & Young's comments with respect to the types of property to which Ernst and Young's comments would apply. Staff stated that it would discuss with Ernst and Young to obtain clarification.

**Committee Action:**

Upon motion by Mr. Horton, seconded by Ms. Steel, the Committee unanimously approved staff's recommendation to continue to work with interested parties to discuss the application of tax to prewritten software.

/s/ Betty T. Yee

Honorable Betty T. Yee, Committee Chair

/s/ Cynthia Bridges

Cynthia Bridges, Executive Director

BOARD APPROVED

at the February 26, 2013 Board Meeting

/s/ Joann Richmond

Joann Richmond, Chief  
Board Proceedings Division

**Regulation 4601. Service of a Notice of Violation or Warning Notice**

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law. The Notice of Suspension, Notice of Revocation, Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub-post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.



## Regulation 4603. Penalties for Licensed or Unlicensed Retailers

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).
- (2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision (b)).
- (4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

**(b)** A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

- (1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).
- (2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

**(d)** A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

- (1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.
- (2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.
- (3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.
- (4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

**(e)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

**(f)** Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

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**Regulation 4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).

(2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).

(3) Business and Professions Code section 22978.5, subdivision (b) (distributor's or wholesaler's failure to retain sales records).

(4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

**(b)** A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision. (b)).

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

**(d)** A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

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(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

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**Regulation 4605. Penalties for Licensed or Unlicensed Manufacturers and Importers**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:

**(a)** A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).

(2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).

(3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).

(4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).

(5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

**(b)** A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subdivision. (b)) shall result in a 20-day suspension.

**(c)** A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

**(d)** In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

**(e)** Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4, 22978.6, or~~ 22980.3, subdivision (a)(2) or subdivision (d).

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**Regulation 1685.5. Calculation of Estimated Use Tax – Use Tax Table.**

*Reference:* Section 6452.1, Revenue and Taxation Code.

**(a) In General.**

(1) Estimated Use Tax and Use Tax Table. The Board of Equalization (BOE) is required to annually calculate the estimated amount of use tax due according to a person's adjusted gross income (AGI) and make such amounts available to the Franchise Tax Board (FTB), by July 30 of each year, in the form of a use tax table for inclusion in the instructions to the FTB's returns.

**(2) Who is Eligible to Use BOE Use Tax Tables.**

(A) Consumers may elect to use the use tax tables included in the instructions to their FTB returns to report their estimated use tax liabilities for one or more single nonbusiness purchases of individual items of tangible personal property each with a sales price of less than one thousand (\$1,000) on their FTB returns. However, eligible consumers may still calculate their actual use tax liabilities using the worksheets in the instructions to their FTB returns and report their actual use tax liabilities on their FTB returns. Consumers are not required to use the use tax tables included in the instructions to their FTB returns.

(B) The use tax table may not be used to estimate use tax liabilities for business purchases, including purchases made by businesses required to hold a seller's permit or to register with the BOE under the Sales and Use Tax Law and report their use tax liabilities directly to the BOE.

(3) Safe Harbor. If eligible consumers use the use tax tables included in the instructions to their FTB returns to estimate their use tax liabilities for qualified nonbusiness purchases and correctly report their estimated use tax liabilities for their qualified nonbusiness purchases in accordance with their AGI ranges, then the BOE may not assess the difference, if any, between the estimated use tax liabilities reported in accordance with the use tax tables and the consumers' actual use tax liabilities for qualified nonbusiness purchases.

**(b) Definitions and Data Sources.**

(1) AGI Ranges. The use tax table shall be separated into fifteen (15) AGI ranges as follows:

- (A) AGI less than \$10,000;
- (B) AGI of \$10,000 to \$19,999;
- (C) AGI of \$20,000 to \$29,999;
- (D) AGI of \$30,000 to \$39,999;
- (E) AGI of \$40,000 to \$49,999;
- (F) AGI of \$50,000 to \$59,999;
- (G) AGI of \$60,000 to \$69,999;

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- (H) AGI of \$70,000 to \$79,999;
- (I) AGI of \$80,000 to \$89,999;
- (J) AGI of \$90,000 to \$99,999;
- (K) AGI of \$100,000 to \$124,999;
- (L) AGI of \$125,000 to \$149,999;
- (M) AGI of \$150,000 to \$174,999;
- (N) AGI of \$175,000 to \$199,999;
- (O) AGI more than \$199,999

(2) Use Tax Liability Factor or Use Tax Table Percentage. For the 2011 calendar year the use tax liability factor or use tax table percentage shall be 0.070 percent (.0007). On June 1, 2012, ~~and each June 1 thereafter~~, the BOE shall calculate the use tax liability factor or use tax table percentage for the current calendar year by multiplying the percentage of income spent on taxable purchases for the preceding calendar year by 0.37, multiplying the product by the average state, local, and district sales and use tax rate, and then rounding the result to the nearest thousandth of a percent. On June 1, 2013, and each June 1 thereafter, the BOE shall calculate the use tax liability factor or use tax table percentage for the current calendar year by multiplying the percentage of income spent on taxable purchases for the preceding calendar year by 0.23, multiplying the product by the average state, local, and district sales and use tax rate, and then rounding the result to the nearest thousandth of a percent.

(3) Total Personal Income. Total personal income shall be determined by reference to the most current personal income data published by the United States Bureau of Economic Analysis.

(4) Total Spending at Electronic Shopping and Mail Order Houses. Total spending at electronic shopping and mail order houses shall be determined by reference to the most current electronic shopping and mail order house spending data published by the United States Census Bureau.

(5) Total Spending on Taxable Purchases. Total spending on taxable purchases shall be determined by:

(A) Determining the percentage, rounded to the nearest tenth of a percent, of total spending at electronic shopping and mail order houses that are not included in the following categories of items, by reference to the most current retail trade product lines statistics by kind of business data published by the United States Census Bureau:

- (i) Groceries and other foods for human consumption off premises, excluding bottled, canned, or packaged soft drinks;
- (ii) Prescriptions;
- (iii) Video Content Downloads;
- (iv) Audio Content Downloads;

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(v) Prepackaged computer software, including software downloads; and

(vi) All nonmerchandise receipts.

(B) Adding ten billion dollars (\$10,000,000,000) to the total spending at electronic shopping and mail order houses to account for spending that is not included in the spending data published by the United States Census Bureau; and

(C) Multiplying the sum calculated in (B) by the percentage of total spending at electronic shopping and mail order houses that are not included in the categories of items listed in (A) above so that the result does not include spending on nontaxable purchases, and then rounding the result to the nearest tenth of a percent.

(6) Percentage of Income Spent on Taxable Purchases. The percentage of income spent on taxable purchases during a calendar year shall be calculated by dividing the total spending on taxable purchases for that year by the total personal income for that year, multiplying the result by 100, and rounding the result to the nearest tenth of a percent.

(7) Average State, Local, and District Sales and Use Tax Rate. The average state, local, and district sales and use tax rate for a calendar year shall be the total of:

(A) The rates of the statewide sales and use taxes imposed under section 35 of article XIII of the California Constitution and the Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.) in effect on January 1 of that year;

(B) The statewide rate of local tax imposed under the Bradley-Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code, § 7200 et seq.) in effect on January 1 of that year; and

(C) The weighted average rate of the district taxes imposed under the Transactions and Use Tax Law (Rev. & Tax Code, § 7251 et seq.) in effect in the various jurisdictions throughout the state on January 1 of that year after taking into account the proportion of the total statewide taxable transactions (by dollar) reported for each jurisdiction during the fourth quarter of the calendar year that is two years prior to the calendar year for which the calculation is made. For example, the total reported taxable transactions (by dollar) for the fourth quarter of 2010 shall be used to determine the weighted average rate of the district tax rates in effect on January 1, 2012, to calculate the weighted average rate of district taxes for calendar year 2012.

(c) Calculation of the Estimated Use Tax Liability.

(1) The estimated use tax liability for the AGI range described in subdivision (b)(1)(A) shall be determined by multiplying \$5,000 by the use tax liability factor or use tax table percentage and then rounding the result to the nearest whole dollar.

(2) The estimated use tax liability for the AGI ranges described in subdivision (b)(1)(B) through (N) shall be determined by multiplying the midpoint of each AGI range by the use tax liability factor or use tax table percentage and then rounding the result to the nearest whole dollar.

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(3) The estimated use tax liability for the AGI range described in subdivision (b)(1)(O) shall be determined by multiplying each range members actual AGI by the use tax liability factor or use tax table percentage and then rounding the result to the nearest whole dollar.

(d) Use Tax Table Format.

(1) The use tax table for calendar year 2011 shall provide as follows:

Adjusted Gross Income (AGI) Range	Use Tax Liability
Less Than \$20,000	\$7
\$20,000 to \$39,999	\$21
\$40,000 to \$59,999	\$35
\$60,000 to \$79,999	\$49
\$80,000 to \$99,999	\$63
\$100,000 to \$149,999	\$88
\$150,000 to \$199,999	\$123
More than \$199,999 -Multiply AGI by 0.070% (.0007)	

(2) The use tax tables for calendar year 2012 and subsequent years shall utilize the same format as follows:

Adjusted Gross Income (AGI) Range	Use Tax Liability
Less Than \$10,000	\$
\$10,000 to \$19,999	\$
\$20,000 to \$29,999	\$
\$30,000 to \$39,999	\$
\$40,000 to \$49,999	\$
\$50,000 to \$59,999	\$
\$60,000 to \$69,999	\$
\$70,000 to \$79,999	\$
\$80,000 to \$89,999	\$
\$90,000 to \$99,999	\$
\$100,000 to \$124,999	\$
\$125,000 to \$149,000	\$
\$150,000 to \$174,999	\$
\$175,000 to \$199,999	\$
More than \$199,999 -Multiply AGI by % (.000 )	

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.





STATE BOARD OF EQUALIZATION

PROPERTY AND SPECIAL TAXES DEPARTMENT

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BETTY T. YEE  
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MICHELLE STEEL  
Third District, Orange County

JEROME E. HORTON  
Fourth District, Los Angeles

JOHN CHIANG  
State Controller

CYNTHIA BRIDGES  
Executive Director

January 4, 2013

Dear Interested Party:

Enclosed are the Agenda, Issue Paper, and Revenue Estimate for the January 15, 2013, Business Taxes Committee (BTC) meeting. This meeting will address proposed Regulation 4801, *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person* and request publication of amendments to Regulations 4601, 4603, 4604 and 4605, approved at the June 26, 2012, BTC meeting.

Action 1 on the Agenda concerns proposed Regulation 4801 of the Cigarette and Tobacco Products Licensing Act (Act) which formalizes the Board's current policy and documentation requirements on transfers of cigarettes and tobacco products between retail stores owned by the same person.

Action 2 on the Agenda concerns approved amendments to Regulation 4601, *Service of a Notice of Violation or Warning Notice*, and Regulations 4603, 4604 and 4605 which provide Board staff additional flexibility in setting suspension periods for violations of the Act when mitigating circumstances are present.

Please feel free to publish this information on your website or otherwise distribute it to your associates, members, or other persons that may be interested in these issues. Thank you for the input on these issues and I look forward to seeing you at the Business Taxes Committee meeting at 10:00 a.m. on **January 15, 2013**, in Room 121 at the address shown above.

Sincerely,

David J. Gau, Deputy Director  
Property and Special Taxes Department

DJG:pb

Enclosures

cc: (all with enclosures)

Honorable Jerome E. Horton, Chairman, Fourth District (MIC 72)  
Honorable Michelle Steel, Vice Chair, Third District (MIC 77)  
Honorable Betty T. Yee, Member, First District (MIC 71)  
Senator George Runner (Ret.), Member, Second District (MIC 78)  
Honorable John Chiang, State Controller, c/o Ms. Marcy Jo Mandel

(via email)

Mr. Robert Thomas, Board Member's Office, Fourth District  
Mr. Joel Angeles, Board Member's Office, Third District  
Mr. Neil Shah, Board Member's Office, Third District  
Mr. Tim Treichelt, Board Member's Office, Third District  
Mr. Alan LoFaso, Board Member's Office, First District  
Ms. Mengjun He, Board Member's Office, First District  
Ms. Yvette Stowers, Board Member's Office, First District  
Mr. Andrew Jacobson, Board Member's Office, First District  
Mr. Sean Wallentine, Board Member's Office, Second District  
Mr. James Kuhl, Board Member's Office, Second District  
Mr. Lee Williams, Board Member's Office, Second District  
Ms. Natasha Ralston Ratcliff, State Controller's Office  
Ms. Cynthia Bridges  
Mr. Randy Ferris  
Ms. Lynn Bartolo  
Mr. Robert Tucker  
Mr. Stephen Smith  
Mr. Todd Gilman  
Mr. Randy Silva  
Mr. Bill Benson  
Ms. Kirsten Stark  
Ms. Debbie Kalfsbeek  
Mr. Phillip Bishop  
Ms. Lynn Whitaker  
Mr. Barry Ivy

**AGENDA —January 15, 2013 Business Taxes Committee Meeting**  
***Proposed Regulation 4801 Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

<p><b>Action 1 — Proposed Regulation 4801, Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person.</b></p> <p>Agenda, page 2 Issue Paper Alternative 1, Item 1</p> <p>Issue Paper Alternative 2, Item 1</p>	<p>Approve and authorize publication of:</p> <p>Staff's proposed Regulation to provide for transfers of cigarettes and tobacco products between retail stores owned by the same legal entity that are supported by a transfer log or similar document and copies of invoices to be maintained at each location participating in the transfer.</p> <p style="text-align: center;">OR</p> <p>Alternatively, direct staff to draft a proposed Regulation that prohibits the transfer of cigarettes and tobacco products between any retail stores regardless of the ownership.</p>
<p><b>Action 2 — Authorize Publication of Amendments Approved at the June 26, 2012, BTC Meeting to Regulations 4601, Service of a Notice of Violation or Warning Notice, 4603, Penalties for Licensed or Unlicensed Retailers, 4604, Penalties for Licensed or Unlicensed Wholesalers and Distributors, and 4605, Penalties for Licensed or Unlicensed Manufacturers and Importers</b></p> <p>See June 26, 2012, BTC minutes <a href="http://www.boe.ca.gov/meetings/pdf/062612.pdf">http://www.boe.ca.gov/meetings/pdf/062612.pdf</a></p>	

**AGENDA — January 15, 2013 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person**

Action Item	Regulatory Language Proposed by Staff
<p><b>Action 1 - Proposed Regulation 4801</b></p>	<p>(a) <u><b>GENERAL.</b> Every retailer of cigarettes and tobacco products is required to maintain purchase invoices for all cigarettes and tobacco products purchased and make those invoices available for inspection by the Board or a law enforcement agency. A licensed retailer owning multiple locations who wishes to transfer cigarettes and tobacco products between its licensed locations shall prepare a transfer log or document at the time of transfer and maintain the records for four years from the date of transfer. A copy of the transfer log or document, accompanied by a copy of the original purchase invoice(s) documenting the purchase of each item transferred, must be kept at both the transferring and receiving locations involved in the transfer for at least one year after the transfer. These transfer logs or documents will be utilized by Board staff for inventory reconciliation and must be provided upon request at the time of the inspection. Copies of original purchase invoices may be maintained at the receiving location on alternative storage media as prescribed in Regulation 4901 (h). The taxpayer must provide facilities and equipment for reading, locating, and reproducing any invoices maintained on alternative storage media.</u></p> <p>(b) <u><b>SPECIFIC APPLICATION.</b> The transfer log or document shall show the following:</u></p> <p>(1) <u>The transferring retail location, license information, supplier's name, invoice number, and the date the bulk cigarettes and tobacco products purchase was made;</u></p> <p>(2) <u>The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and,</u></p> <p>(3) <u>A legible itemized listing of cigarettes and tobacco products transferred using the description as found on the original invoice, including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.</u></p>

**AGENDA — January 15, 2013 Business Taxes Committee Meeting**  
**Proposed Regulation 4801 Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person**

Action Item	Regulatory Language Proposed by Staff
<b>Action 1 cont.</b>	<p>(c) <u>The transfer of cigarettes and tobacco products shall only be allowed when the legal entity licensed as the retailer for the retail location transferring the cigarettes and tobacco products is the same legal entity that is licensed as the retailer at the retail location receiving the cigarettes and tobacco products. As an example, a transfer between a location licensed as a sole proprietorship and a location licensed as a partnership where the sole proprietor is one of the partners would not qualify under this section since the same legal entity does not own both locations. As another example, a transfer between a location licensed to a parent corporation and a location licensed to its wholly owned subsidiary corporation would not qualify under this section since the parent corporation and its wholly owned subsidiary corporation are separate legal entities.</u></p> <p>(d) <u>Records of the transfer shall be made available to the Board or its authorized representative for examination upon request. Failure to provide such documentation when requested can result in the seizure of the cigarettes or tobacco products that are claimed to be transferred and the issuance of a citation. Transfer logs or documents not provided upon request at the time of inspection, or created or provided during or after an inspection has commenced, or created or provided after a seizure and/or citation are not acceptable and cannot be used for the return of seized product or dismissal of a violation.</u></p>

Issue Paper Number **12-009**



- ☐ Board Meeting
- ☒ Business Taxes Committee
- ☐ Customer Services and Administrative Efficiency Committee
- ☐ Legislative Committee
- ☐ Property Tax Committee
- ☐ Other

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## **Proposed Regulation 4801, *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

### **I. Issues**

Should the Board of Equalization (Board) authorize publication of a new regulation, under the Cigarette and Tobacco Products Licensing Act (Act), to provide guidelines on the documentation and retention requirements for transfers of cigarettes and tobacco products between retail stores owned by the same legal entity?

### **II. Alternative 1 - Staff Recommendation**

#### **Item 1 - Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Staff recommends the approval of proposed Regulation 4801 regarding transfers of cigarettes and tobacco products between retail stores owned by the same person. Approving the proposed regulation provides Board staff and licensed retailers who own multiple locations with regulatory guidance for satisfying the documentation and invoice requirements required by statute in order to establish the tax-paid status of the product being transferred. See Exhibit 2 for staff's proposed regulation.

### **III. Other Alternative(s) Considered**

#### **Item 1 - Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Consider approving a regulation prohibiting the transfer of any cigarettes or tobacco products between retail locations owned by the same person, thereby creating a "bright line" prohibiting transfers as recommended by some Interested Parties.

#### IV. Background

On October 12, 2003, the State of California enacted the Cigarette and Tobacco Products Licensing Act (Assembly Bill 71, Horton [Chapter 890, Statutes 2003]) which established a statewide licensing program under Division 8.6 (commencing with Section 22970) of the Business and Professions Code (B&P Code). The Act imposes licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. Assembly Bill 1749 (Chapter 501, Statutes 2006) added the same licensing requirements to manufacturers and importers of tobacco products. These licensing requirements are in addition to other permits and licenses that may be required depending on a person's business operations. The Act intended to address the problem of untaxed distributions and illegal sales of cigarettes and tobacco products in California and includes provisions for new recordkeeping requirements, identifies violations that may result in license suspensions or revocations including the imposition of civil and criminal penalties, and authorizes Board staff to inspect and seize any untaxed cigarettes or tobacco products. Inspections are performed by the Board's Investigations Division (ID) staff and, based upon the findings during the course of their inspections, may result in the issuance of citations and penalties for violations.

The Act authorizes the Board to administer and enforce the provisions of the Act and to prescribe, adopt, and enforce rules and regulations relating to its administration and enforcement. Since the inception of the Act, the Board has prescribed and adopted regulations to clarify the provisions with the intent to uniformly administer and enforce the provisions of the Act, and to provide guidance and clarity of the Act's provisions to licensed and unlicensed cigarette and tobacco product retailers, wholesalers, distributors, manufacturers, and importers.

Based on recent citations and related appeals proceedings involving the seizure of cigarettes and tobacco products due to a retailer's failure to maintain documentation supporting an assertion that tax-paid product was transferred from one licensed retail location to another licensed retail location owned by the same legal entity, the Special Taxes and Fees Division was asked to develop a new regulation to formalize the Board's existing policies regarding documentation requirements for the transfer of cigarettes and tobacco products between licensed retail locations owned by the same legal entity. Transfers of cigarettes and tobacco products between licensed retail locations owned by the same legal entity excludes sales transactions of cigarettes and tobacco products between licensed retail locations which are expressly prohibited by Revenue and Taxation Code (R&T Code) section 30478.

In April 2011, Board staff provided guidance to licensees and staff on its current transfer policies through an update to Publication 78, *Sales of Cigarettes and Tobacco Products in California*, and a letter sent to 1,790 legal entities owning multiple cigarette and tobacco products licensed retail locations. Both the letter and Publication 78 provided that:

"Generally, the transfer of cigarettes and tobacco products are not permitted. However, if you own more than one store and licenses are held by the same legal entity, you may be allowed to transfer cigarettes and tobacco products between stores belonging to the same legal entity. When transferring cigarettes and tobacco products, legible transfer records and copies of the original purchase invoice must be kept at each location involved in the transfer. Such transfer records which must be prepared at the time of transfer, must include the address of each store, the purchase invoice date, the purchase invoice number, the supplier's name on the invoice, including type of packaging, flavor and or style, and the

amounts of items transferred. Failure to provide such documentation when requested can result in the seizure of the claimed transferred product.”

The above guidance represents the basis for the proposed Regulation.

Interested Parties (IP) meetings were held on March 6, 2012, and May 4, 2012. Divergent positions were taken by SEIU Local 1000, representing Business Taxes Specialists and Business Taxes Compliance Specialists in the Investigation Division,<sup>1</sup> and Mr. Dennis Loper, representing the California Distributors Association, who both opposed allowing transfers, and Mr. Scott Louie representing Chevron, and Mr. Ron Michelson, owner of two Briar Patch smoke shops, who both support allowing transfers. Those opposed to allowing transfers argue that the Act does not allow transfers and that only those cigarette and tobacco products sold to the licensed retailer store location may be sold at that licensed location. Those in support of allowing transfers argue that the Act does not specifically prevent transfers and not allowing transfers of cigarette and tobacco product between stores owned by the same person adds an undue burden on retailers owning more than one retail store. For a full discussion on the two IP meetings, please see the Issue Paper presented at the June 26, 2012, BTC meeting at: <http://www.boe.ca.gov/meetings/pdf/IP-Cigarette.pdf>.

Although the Act does not specifically provide for transfers of cigarette and tobacco products between retail locations owned by the same person, the Act does not preclude such transfers either. Mr. Steven Alari representing SEIU Local 1000, acknowledged at the May 4, 2012, IP meeting that there are no provisions in the Act that specifically preclude transfers. The Act requires that a retailer of cigarettes or tobacco products obtain a retailer’s license for each retail location in which cigarettes or tobacco products are sold, maintain purchase invoices that meet the requirements set forth in section 22978.4 of the B&P Code for all cigarettes or tobacco products the retailer purchased for a period of four years and that these records be maintained at the retail location for at least one year after purchase. Section 22978.4 also prescribes form and content requirements for invoices issued by distributors and wholesalers. Besides requiring distributor and wholesaler information, each invoice must contain the name, address and license number of the customer, an itemized listing of cigarette and tobacco products sold, date of sale, and the amount of excise taxes due to the Board by the distributor or a statement that reads: “All California cigarette and tobacco product taxes are included.”

A retail location is defined under section 22971 (q) of the Act as any building from which cigarettes or tobacco products are sold at retail, or a vending machine. “Sale” is defined in Section 30006 of the R&T Code as any transfer of title or possession for consideration, exchange or barter, in any manner or by any means whatever. As a result, the Act does not require a retailer to maintain a license at a warehouse or storage location from which retail sales are not made. The Act also does not require that a distributor or wholesaler deliver only to the address of the licensed retail location. Section 22978.4 (a)(4) requires that a distributor or wholesaler include on any invoice the name, address, and license number of the retailer, distributor, or wholesaler to whom cigarettes or tobacco products are sold. It does not require that the product be delivered to the address where the retail license is held. There would appear to be good reasons for not requiring such a limitation, as had such a requirement been included in the Act, traditional cash and carry purchases would be prohibited, and vending machine operators would only be able to take delivery at the location of a licensed vending machine, which is generally located at another person’s business. One could therefore make an argument that without such delivery limitations the Act contemplates transfers of cigarettes and tobacco products between retail or storage locations owned by the same legal entity so long as the invoice retention requirements are satisfied at each retail location.

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<sup>1</sup> The initial position taken by SEIU Local 1000 was not supported by ID management who supports and actively participated in the drafting of proposed Regulation 4801.



## **IV. Discussion**

At the June 26, 2012 BTC meeting, staff presented proposed Regulation 4801, and requested the Board's approval and authorization to publish the proposed Regulation in order to begin formal rulemaking. Mr. Alari, representing SEIU Local 1000, was the sole public speaker. Mr. Alari reiterated his position that the Board should prohibit transfers thereby creating a "bright line" for ID staff to follow when performing inspections. Mr. Alari noted that allowing transfers further complicates the reconciling of the tobacco product purchases to the tax-paid invoices during an inspection and thereby makes it more difficult to identify evasion of the cigarette and tobacco products excise taxes. While some Board Members expressed support for staff's proposed regulation, there were also concerns raised that the regulation may not be clear in what constitutes "same legal entity." In addition, concerns were raised regarding the need for adequate inventory controls when transferring products in order to prevent the blending of tax-paid and ex-tax product and to provide ID inspectors with the documents necessary to reconcile the tobacco product inventory to their original purchase invoices in order to verify the tax-paid or ex-tax status of the product. Enhancements were also suggested to the sample transfer log to include all the required elements in the proposed regulation that are necessary to satisfy the inspectors. Therefore the matter was held over and staff was directed to work with ID and interested parties to further address these concerns in the regulation and the sample transfer log.

### **Same Legal Entity/Same Person**

Legal entity is used in the regulation to more clearly convey the statutory definition of "person" in the Act. Person is defined in section 22971 (n) of the Act to mean a person as defined in section 30010 of the R&T Code which includes any individual, firm, partnership, joint venture, limited liability company, association, social club, fraternal organization, corporation, estate, trust, business trust, receiver, trustee, syndicate, this state, any county, city and county, municipality, district, or other political subdivision of the state, or any other group or combination acting as a unit. Person is commonly defined to include an individual man, woman, or child and is not commonly thought of in the context of the definition above, whereas, "legal entity" conveys a broader meaning, more in line with the legal definition for "person" in the Act. For purposes of the regulation "same legal entity" was used in place of "same person" to better convey the R&T Code definition of "Person."

Because of the misconception that could arise in situations involving transfers between sole proprietors and partnerships where the sole proprietor is also a partner, Regulation 4801(c) provides a specific example to address this non-qualifying transfer. To provide additional clarity and address situations involving a parent corporation making a non-qualifying transfer to its wholly owned subsidiary, another potentially problematic scenario, staff added another example to Regulation 4801(c) specifically addressing this non-qualifying situation. The following underlined changes to 4801(c) are recommended to provide additional clarity to what is meant by "same legal entity":

(c) The transfer of cigarettes and tobacco products shall only be allowed when the legal entity licensed as the retailer for the retail location transferring the cigarettes and tobacco products is the same legal entity that is licensed as the retailer at the retail location receiving the cigarettes and tobacco products. As an example, a transfer between a location licensed as a sole proprietorship and a location licensed as a partnership where the sole proprietor is one of the partners would not qualify under this section since the same legal entity does not own both locations. As another example, a transfer between a location licensed to a parent corporation and a location licensed to its wholly owned subsidiary

corporation would not qualify under this section since the parent corporation and its wholly owned subsidiary corporation are separate legal entities.

### **Inventory Control**

A recurring concern for SEIU Local 1000 is that transfers further complicate an already complicated inspection by making it more difficult to reconcile the tobacco product inventory at the location to their original invoices to determine if they were purchased tax-paid from a licensed distributor or wholesaler. The regulation requires a document or transfer log that includes all the essential elements called for in subsection (b) of proposed Regulation 4801 along with a copy of the original invoice to be maintained at both retail locations involved in the transfer for inventory reconciliation purposes. Subsection (b) provides:

- (b) **SPECIFIC APPLICATION.** The transfer log or document shall show the following:
- (1) The transferring retail location, license information, supplier's name, invoice number, and the date the bulk cigarettes and tobacco products purchase was made;
  - (2) The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and
  - (3) A legible itemized listing of cigarettes and tobacco products transferred using the description as found on the original invoice including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.

In an attempt to address SEIU's concern, ID plans to update their Inspection Manual to include a requirement that an Inspector ask at the beginning of the inspection if transfers occur and if they do, to secure the transfer log at that time. Having this information upfront provides the Inspector with the knowledge of what to expect as they conduct the inspection and what will be involved as they reconcile the inventory to the invoices and transfer log at the location. To further stress the requirement that the transfer log be made available at the beginning of the inspection and that these transfer logs are necessary for inventory reconciliation, the following underlined changes are recommended to subsections (a) and (d) of Regulation 4801:

(a) **GENERAL.** Every retailer of cigarettes and tobacco products is required to maintain purchase invoices for all cigarettes and tobacco products purchased and make those invoices available for inspection by the Board or a law enforcement agency. A licensed retailer owning multiple locations who wishes to transfer cigarettes and tobacco products between its licensed locations shall prepare a transfer log or document at the time of transfer and maintain the records for four years from the date of transfer. A copy of the transfer log or document, accompanied by a copy of the original purchase invoice(s) documenting the purchase of each item transferred, must be kept at both the transferring and receiving locations involved in the transfer for at least one year after the transfer. These transfer logs or documents will be utilized by Board staff for inventory reconciliation and must be provided upon request at the time of the inspection. Copies of original purchase invoices may be maintained at the receiving location on alternative storage media as prescribed in Regulation 4901 (h). The taxpayer must provide facilities and equipment for reading, locating, and reproducing any invoices maintained on alternative storage media.

(d) Records of the transfer shall be made available to the Board or its authorized representative for examination upon request. Failure to provide such documentation when requested can result in the seizure of the cigarettes or tobacco products that are claimed to

be transferred and the issuance of a citation. Transfer logs or documents not provided upon request at the time of inspection or created or provided during or after an inspection has commenced, or created or provided after a seizure and/or citation are not acceptable and cannot be used for the return of seized product or dismissal of a violation.

In regard to blending, unfortunately due to the fungible nature of certain types of tobacco products, one invoice for tax-paid product could be used in an attempt to satisfy the invoicing requirements of purchases for tobacco products that were not tax paid. These attempts to evade tax have occurred historically and continue today within this particular industry, primarily with tobacco products because such products are not stamped. Blending may occur whether a person owns one location or multiple locations. Transfers can complicate the reconciliation, but prohibiting transfers will not prevent blending. As an example, if at the location there is never more inventory than there is tax-paid invoice support and the dates of that inventory reconcile with that of the supporting invoices, one would come to the conclusion, without other evidence, that the product on the shelf was tax paid and purchased from a licensed wholesaler or distributor. However, untaxed purchases of the same product from an unlicensed person could be comingled with the tax-paid inventory without raising suspicion so long as the shelf stock never exceeds the amount of inventory supported by tax-paid invoices.

### **Sample Transfer Log**

Following the first IP meeting, it was suggested that an example of a transfer log would be helpful to visually depict what the regulation's required elements contemplated in regard to the documentation needed to support a transfer. The sample transfer log (Exhibit 3) is not a subsection to the regulation but an illustrative example of what a taxpayer may wish to replicate. As noted in the regulation, the taxpayer need only provide a document or transfer log in any format so long as it contains the essential elements as required in subsection (b) of the proposed regulation and is accompanied by a copy of the original invoice in either electronic or hardcopy form. It was noted at the June 26, 2012, BTC meeting that the sample log may not contain a complete enough description of the transferred product in order for ID inspectors to reconcile the tobacco product inventory to the purchase invoices. Staff proposes the following underlined changes to subsection (b)(3) of Regulation 4801:

A legible itemized listing of cigarettes and tobacco products transferred using the description as found on the original invoice including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.

Requiring a description as found on the original invoice allows ID staff to easily identify the transferred product from a variety of products with similar descriptions. This same wording "complete description from original invoice" was incorporated on the sample transfer log under the heading of "Items Transferred." In addition some of the examples were updated with complete invoice descriptions to comply with the requirements.

### **Comments and Summary**

Proposed changes to Regulation 4801 and the Sample Transfer Log were disseminated to interested parties and concerned staff with a request that any comments be returned by August 10, 2012.

As a result of staff's recommended changes to Regulation 4801, Ms. Yvonne Walker, President of SEIU Local 1000, is no longer opposed to the proposed regulation (see Exhibit 4 for copy of letter dated November 29, 2012.)

Mr. Ron Michelson, owner of two Briar Patch smoke shops, commented on the business need for the ability to transfer tobacco products between his two stores in order to meet the needs of customers and

to keep inventory at appropriate levels. “Transferring inventory to the store where it is needed is just good business practice.” Although Mr. Michelson is supportive of the proposed regulation, he expressed some concerns with the transfer log’s format and when product transferred once is transferred again, and in those instances, being able to identify accurate vendor and invoice information. He is also concerned that inspections can occur without notice and if the proprietor or appropriate staff is not available to provide a copy of the transfer log, his tobacco inventory could be confiscated.

With respect to the format of the sample transfer log, any format will suffice so long as the required elements of the regulation are included. This information has been conveyed to Mr. Michelson and has resolved this concern. Subsequent transfers from previously transferred product poses some difficulty in identifying the original invoice from which the product was acquired, but may be remedied by identifying the invoice copy from the original transfer as being the invoice supporting the subsequent transfer. With regard to inspections, unfortunately inspections occur on a random basis without notice. Providing notice would defeat the purpose for the inspection. For instance, if a retailer was notified of an upcoming inspection and this retailer was acquiring cigarettes or tobacco product without the applicable tax they could easily remove the product from their inventory along with the invoices prior to the inspection. Maintaining copies of invoices and transfer logs for one year at the premise are required for any inspection, with or without the regulation and a required business practice in this industry. ID inspectors are known to wait for a period of time for the appropriate personnel to arrive during an inspection, but it is incumbent upon any retailer of cigarettes and tobacco products to have these documents readily available.

To acknowledge the practice of transfers of cigarettes and tobacco products within this industry, the Board has adopted procedures allowing for the transfers of cigarettes and tobacco products between retail locations owned by the same person. These procedures acknowledge the blending concern and are designed to address them through requirements that copies of invoices be maintained at both locations and a transfer log or document be available detailing the amount of product, description of product, and license information of the transferring and receiving locations. Proposed Regulation 4801 is consistent with current Board policies and procedures and is intended to provide for consistent enforcement of the documentary requirement provisions. The proposed regulation will also provide retailers with the documentation and recordkeeping requirements for these types of transfers so as to avoid seizures of the transferred products, along with avoiding citations and fines that may be assessed against the retailer for improper documentation of these transfers.

## **VI. Alternative 1 - Staff Recommendation**

### **Item 1 – Adopt Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

#### **A. Description of Alternative 1**

Regulation 4801 as proposed by staff formalizes the Board’s current policy of allowing transfers of cigarettes and tobacco products between retail stores owned by the same legal entity. It requires that every retailer of cigarettes and tobacco products maintain purchase invoices for all cigarettes and tobacco products purchased and to make those invoices available for inspection by the Board or law enforcement. Licensed retailers owning more than one location may transfer product between locations so long as the retailer prepares a transfer log or other document at the time of transfer and maintains a copy of the transfer log at both the transferring and receiving location along with copies

of applicable invoices for inspection. These records must be maintained for a period of four years with copies of the log and invoices maintained at each location involved in the transfer for a period of one year. Copies of invoices may be maintained on alternative storage media pursuant to Regulation 4901, *Records*. Facilities and equipment must be provided for reading, locating and reproducing any invoices maintained on alternative storage media.

The transfer log or document shall show the following:

- (1) The transferring retail location, license information, supplier's name, invoice number, and date the bulk cigarettes and tobacco products purchase was made;
- (2) The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and
- (3) A legible itemized listing of cigarettes and tobacco products transferred using the description as found on the original invoice, including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.

Proposed regulation is shown in Exhibit 2.

#### **B. Pros of Alternative 1**

- Is consistent with the Board's current policy on transfers.
- Provides regulatory support and guidance to taxpayers and staff.
- Adopts into regulation the retail industry's current business practices regarding transfers between retail stores owned by the same legal entity.

#### **C. Cons of Alternative 1**

- Requires a degree of additional verification during an inspection.
- Requires a taxpayer to prepare and maintain an additional document or log to satisfy the records requirement in section 22974 of the B&P Code.

#### **D. Statutory or Regulatory Change for Alternative 1**

No statutory change is required. However, staff's recommendation does require adoption of proposed Regulation 4801.

#### **E. Operational Impact of Alternative 1**

Minor. Although the regulation adopts current policy, staff intends to add the sample transfer log to the Board's website and appropriate publications for the tobacco industry.

#### **F. Administrative Impact of Alternative 1**

##### **1. Cost Impact**

Absorbable.

##### **2. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).

**G. Taxpayer/Customer Impact of Alternative 1**

None, adopts current policy.

**H. Critical Time Frames of Alternative 1**

None.

**VII. Other Alternatives**

**Item 1 - Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

**A. Description of Alternative**

Direct staff to draft a regulation prohibiting transfers of cigarettes and tobacco products between retail stores regardless of ownership.

**B. Pros of Alternative**

- Limits the invoice documentation required on site to only those invoices referencing the licensed retail location.
- Prohibition creates a “bright line” on transfers for retailers and Board staff to follow.

**C. Cons of Alternative**

- Eliminates a retailer’s ability to transfer product to their own stores regardless of the business situation. For instance, retailers would not be allowed to transfer product from a closed store to one that is still in business or from a store that has overbought a product that can be sold at another location. Retailers would also be prohibited from transferring inventory when a supplier is out of a product that is available at another taxpayer owned location, or when there are supplier delays in delivering a product to one retail store but the product is available at another taxpayer owned location.
- May prevent taxpayers with multiple locations from taking advantage of quantity discounts.

**D. Statutory or Regulatory Change for Alternative**

No statutory change required. However, since the Act does not specifically prohibit the transfer of cigarettes and tobacco products between retail stores owned by the same legal entity, a regulation prohibiting transfers should be considered.

**E. Operational Impact of Alternative**

Prohibiting transfers would require the Board to rescind the letter mailed April 2011 to retailers owning multiple locations that addressed the current policy allowing transfers. Staff would also need to revise Publication 78, *Sales of Cigarettes and Tobacco Products in California*, and advise industry of the policy change in other outreach materials.

**F. Administrative Impact of Alternative**

**1. Cost Impact**

Additional mailing costs unknown.

**2. Revenue Impact**

None.

**G. Taxpayer/Customer Impact of Alternative**

A prohibition of the common practice of transferring cigarettes or tobacco products between a taxpayer's own stores could have a major impact on those retailers operating multiple licensed locations.

**H. Critical Time Frames of Alternative**

None.

**Preparer/Reviewer Information**

Prepared by: Policy and Compliance Division, Property and Special Taxes Department

Current as of: December 5, 2012

REVENUE ESTIMATE

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION



BOARD OF EQUALIZATION  
REVENUE ESTIMATE

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**Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

**I. Issues**

Should the Board of Equalization (Board) authorize publication of a new regulation, under the Cigarette and Tobacco Products Licensing Act (Act), to provide guidelines on the documentation and retention requirements for transfers of cigarettes and tobacco products between retail stores owned by the same legal entity?

**II. ALTERNATIVE 1 - STAFF RECOMMENDATION**

**Item 1 – Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Staff recommends the approval of proposed Regulation 4801 regarding transfers of cigarettes and tobacco products between retail stores owned by the same person. Approving the proposed regulation provides Board staff and licensed retailers who own multiple locations with regulatory guidance for satisfying the documentation and invoice requirements required by statute in order to establish the tax-paid status of the product being transferred. See Exhibit 2 for staff's proposed regulation.

**III. Other Alternative(s) Considered**

**Item 1 – Proposed Regulation 4801 *Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person***

Consider approving a regulation prohibiting the transfer of any cigarettes or tobacco products between retail locations owned by the same person, thereby creating a "bright line" prohibiting transfers, as recommended by some Interested Parties.



**Alternative 1 – Staff Recommendation**

**Item 1:** There is nothing in Item 1 of the staff recommendation that would impact revenue. Regulation 4801 as proposed by staff formalizes the Board's current policy of allowing transfers of cigarettes and tobacco products between retail stores owned by the same legal entity. It requires that every retailer of cigarettes and tobacco products maintain purchase invoices for all cigarettes and tobacco products purchased and to make those invoices available for inspection by the Board or law enforcement. Licensed retailers owning more than one location may transfer product between their licensed locations so long as the retailer prepares a transfer log or other document at the time of transfer and maintain a copy of the transfer log at both the transferring and receiving location along with copies of applicable invoices. These records must be maintained for a period of four years with copies of the log and invoices maintained at each location involved in the transfer for a period of one year. Copies of invoices may be maintained on alternative storage media pursuant to Regulation 4901, *Records*. Facilities and equipment must be provided for reading, locating and reproducing any invoices maintained on alternative storage media.

**Other Alternative(s) Considered**

**Item 1:** There is nothing in Item 1 of the other alternative(s) considered that would impact revenue. This alternative would prohibit transfers of cigarettes and tobacco products between retail stores regardless of ownership.

**Revenue Summary**

Alternative 1:

Item 1 – This alternative does not have a revenue impact.

Other alternatives considered:

Item 1 – This alternative does not have a revenue impact.

**Preparation**

Mr. Bill Benson, Jr., Acting Chief, Research and Statistics Section, Legislative and Research Division, prepared this revenue estimate. Ms. Lynn Bartolo, Chief, Special Taxes, Policy and Compliance Division, Property and Special Taxes Department, reviewed this revenue estimate. For additional information, please contact Mr. Benson at 916-445-0840.

August 20, 2012

Regulation 4801. Transfers of Cigarettes and Tobacco Products between Retail Stores Owned by the Same Person.

Reference: Section 22971, 22974, 22974.3, and 22978.4, Business and Professions Code

(a) GENERAL. Every retailer of cigarettes and tobacco products is required to maintain purchase invoices for all cigarettes and tobacco products purchased and make those invoices available for inspection by the Board or a law enforcement agency. A licensed retailer owning multiple locations who wishes to transfer cigarettes and tobacco products between its licensed locations shall prepare a transfer log or document at the time of transfer and maintain the records for four years from the date of transfer. A copy of the transfer log or document, accompanied by a copy of the original purchase invoice(s) documenting the purchase of each item transferred, must be kept at both the transferring and receiving locations involved in the transfer for at least one year after the transfer. These transfer logs or documents will be utilized by Board staff for inventory reconciliation and must be provided upon request at the time of the inspection. Copies of original purchase invoices may be maintained at the receiving location on alternative storage media as prescribed in Regulation 4901 (h). The taxpayer must provide facilities and equipment for reading, locating, and reproducing any invoices maintained on alternative storage media.

(b) SPECIFIC APPLICATION. The transfer log or document shall show the following:

- (1) The transferring retail location, license information, supplier's name, invoice number, and the date the bulk cigarettes and tobacco products purchase was made;
- (2) The receiving retail location(s), license information, and date the cigarettes and tobacco products were transferred; and,
- (3) A legible itemized listing of cigarettes and tobacco products transferred using the description as found on the original invoice including packaging (e.g., 20 5-packs; 60-ct boxes), flavor and/or style, and quantity transferred.

(c) The transfer of cigarettes and tobacco products shall only be allowed when the legal entity licensed as the retailer for the retail location transferring the cigarettes and tobacco products is the same legal entity that is licensed as the retailer at the retail location receiving the cigarettes and tobacco products. As an example, a transfer between a location licensed as a sole proprietorship and a location licensed as a partnership where the sole proprietor is one of the partners would not qualify under this section since the same legal entity does not own both locations. As another example, a transfer between a location licensed to a parent corporation and a location licensed to its wholly owned subsidiary corporation would not qualify under this section since the parent corporation and its wholly owned subsidiary corporation are separate legal entities.

(d) Records of the transfer shall be made available to the Board or its authorized representative for examination upon request. Failure to provide such documentation when requested can result in the seizure of the cigarettes or tobacco products that are claimed to be transferred and the issuance of a citation. Transfer logs or documents not provided upon request at the time of inspection, or created or provided during or after an inspection has commenced, or created or provided after a seizure and/or citation are not acceptable and cannot be used for the return of seized product or dismissal of a violation.

**Sample Transfer Log  
Cigarettes and Tobacco Products**

<b>Store Transferring Product</b>	<b>Store Receiving Product</b>	<b>Date of Transfer</b>	<b>Items Transferred Complete Description From Original Invoice</b>	<b>Original Purchase From</b>
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	B Street Market 123 B Street Anywhere, CA LRQ 91-1XXXXX	March 2, 2010	50 packs Marlboro cigarettes Red Hard Pack, 100 5 boxes Romeo y Juliet Reserve Real Churchill Cigars (25ea)	LD Tobacco Distributors LDG 90-2XXXXX February 14, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	B Street Market 123 B Street Anywhere, CA LRQ 91-1XXXXX	April 30, 2010	7 rolls Grizzly Long Cut, Mint (5ea) 2 packs Black & Mild cigars, wine flavor (5ea) 3 packs Black & Mild cigars, wine flavor, wood tip (5ea)	S&W Wholesale SWQ 90-3XXXXX April 27, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	D Street Market 123 D Street Anywhere, CA LRQ 91-3XXXXX	June 28, 2010	50 packs Marlboro Cigarettes Red King 12 packs Backwoods Sweet (6ea) 6 rolls Copenhagen Regular (5ea)	Tobacco Road Distributors SWQ 90-4XXXXX June 12, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	C Street Market 123 C Street Anywhere, CA LRQ 91 2XXXXX	August 15, 2010	8 packs Swisher Cigarillo wood tip (5ea) 10 boxes Salem Gold 100	S&W Wholesale SWQ 90-3XXXXX July 21, 2010
D Street Market 123 D Street Anywhere, CA LRQ 91-3XXXXX	A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	August 28, 2010	6 packs Backwoods Sweet (6ea)	Tobacco Road Distributors SWQ 90-4XXXXX June 12, 2010
A Street Market 123 A Street Anywhere, CA LRQ 91-0XXXXX	E Street Market 123 E Street Anywhere, CA LRQ 91 4XXXXX	October 3, 2010	20 packs Marlboro Cigarettes Gold 100 2 rolls Skoal Long Cut Mint (5ea) 2 rolls Skoal Bandit Wintrg. (5ea)	LD Tobacco Distributors LDG 90-2XXXXX September 29, 2010

**Note:** Transfer of cigarettes and tobacco products is allowed only when the legal ownership (as registered with the BOE) of the store transferring the product is the same as the legal ownership of the store receiving the product.

**For example:**

<b>Store Transferring Product</b>	<b>Store Receiving Product</b>	<b>Is the Transfer Allowed?</b>
John Smith –sole proprietor	John Smith – sole proprietor	Yes
John Smith – sole proprietor	John Smith – corporate officer	No
John Smith – sole proprietor	John Smith – partner	No
John Smith Corporation – Parent Corp.	John Smith Jr. – Wholly Owned Sub.	No



November 29, 2012

The Honorable Jerome Horton, Chair  
California State Board of Equalization  
Sacramento Headquarters Office  
450 N Street, MIC:72  
Sacramento, CA 95814

YVONNE R. WALKER  
President

M. CORA OKUMURA  
Vice President  
and Secretary-Treasurer

TAMEKIA N. ROBINSON  
Vice President  
for Organizing/Representation

MARGARITA MALDONADO  
Vice President for Bargaining

Chairman Horton:

SEIU Local 1000, representing the Business Taxes Specialists and Business Taxes Compliance Specialists in the Investigation Division at the Board of Equalization, writes to inform you of our removal of concerns relating to the Proposed Regulation 4801.

The newly revised Regulation 4801 improves upon the inventory controls that BOE investigators will have at their disposal to ensure excise taxes are being properly paid. We appreciate the Board's willingness to work with our highly skilled and knowledgeable members at the BOE to ensure that California has the best tools and regulations on the books to ensure retailers have a level playing field from which to work.

On behalf of all our members at SEIU Local 1000, we appreciate the Board's work.

Sincerely,

YVONNE R. WALKER  
President

SERVICE EMPLOYEES  
INTERNATIONAL UNION

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cc: Honorable Betty Yee, First District  
Honorable Michelle Steel, Third District  
Honorable George Runner, Second District  
Honorable John Chiang, State Controller

BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION

450 N STREET

SACRAMENTO, CALIFORNIA

REPORTER'S TRANSCRIPT

JANUARY 15, 2013

BUSINESS TAXES COMMITTEE

REPORTED BY: Kathleen Skidgel

CSR NO. 9039.

Juli Price Jackson.

CSR NO. 5214

P R E S E N T

For the Committee:

Betty T. Yee  
Chair

Michelle Steel  
Member

Jerome E. Horton  
Member

George Runner  
Member

Marcy Jo Mandel  
Appearing for John  
Chiang, State Controller  
(per Government Code  
Section 7.9)

Joann Richmond  
Chief  
Board Proceedings Division

Board of Equalization  
Staff:

Susanne Buehler  
Chief, Tax Policy Division  
Phil Bishop  
Business Taxes Specialist III  
Property and Special Taxes  
Division

Stephen Smith  
Tax Counsel IV  
Legal Department

Bradley Heller  
Tax Counsel IV  
Legal Department

---oOo---

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450 N STREET  
SACRAMENTO, CALIFORNIA  
JANUARY 15, 2013

---oOo---

MR. HORTON: Okay. Ms. Richmond?

MS. RICHMOND: Our next item is the Business  
Taxes Committee. Ms. Yee is the Chair of that  
committee.

Ms. Yee.

MS. YEE: Thank you, Ms. Richmond.

Call the Business Taxes Committee to order. We  
have three items on the, uh, Business Taxes Committee  
agenda; we will take them up in order, and we do have  
speakers on each of the items.

The first item is, uh -- excuse me. The first  
item is proposed Regulation, uh, 4801 related to  
transfers of cigarettes and tobacco products between  
retail stores owned by the same person.

We have several speakers on this item. If I  
could have them come up and be seated. Mr. Steven  
Alari. And, uh, I think I saw Mr. Loper here. Come  
forward.

And, uh, while you're doing so, let me have  
staff introduce the issue.

Good afternoon.

MS. BUEHLER: Good afternoon. I am Susanne  
Buehler with the Sales and Use Tax Department.

We have three agenda items for your



1 consideration this afternoon. They include the Special  
2 Taxes Cigarette and Tobacco Products Licensing Act  
3 regulations; the use tax table; and technology transfer  
4 agreements. We will take each agenda item and their  
5 respective action time separately before moving to the  
6 next one.

7 For agenda item one, with me are Stephen Smith  
8 from our Legal Department and Phil Bishop from our  
9 Property and Special Taxes Department.

10 In action one we ask that the Board approve and  
11 authorize for publication either staff's recommendation  
12 to publish proposed Regulation 4801, transfers of  
13 cigarettes and tobacco products between retail stores  
14 owned by the same person. The regulation would provide  
15 for transfers of cigarettes and tobacco products between  
16 retail stores owned by the same legal entity that are  
17 supported by a transfer log or similar document and  
18 copies of invoices to be maintained at each location  
19 participating in the transfer.

20 Alternative one is embraced by retailers of  
21 cigarettes and tobacco products with multiple locations  
22 and formalizes the Board's current policies regarding  
23 documentation requirements for the transfer of  
24 cigarettes and tobacco products between retail stores  
25 owned by the same person.

26 Or, alternatively, direct staff to draft a  
27 proposed regulation that prohibits the transfer of  
28 cigarette and tobacco products between any retail

1 stores, regardless of the ownership, as recommended by  
2 some interested parties. Language was not submitted by  
3 the interested parties for this alternative.

4 As you noted, we have speakers for action one,  
5 and we are happy to answer any questions you may have.

6 MS. YEE: Thank you, Ms. Buehler.

7 Let's go to the speakers. You'll have two  
8 minutes each. If you'll introduce yourself for the  
9 record and, uh, proceed.

10 Mr. Loper.

11 ---oOo---

12 DENNIS LOPER

13 ---oOo---

14 MR. ALARI: You first.

15 MR. LOPER: Uh, Dennis Loper representing the  
16 California Distributors Association. I apologize that  
17 my daughter had to leave, so you get the worst half of  
18 the organization.

19 Uh, we -- you know, we oppose option one and  
20 support option two. We believe that -- that option one,  
21 although well-meaning, does not protect the Board or the  
22 taxpayers from giving easier ways for blending of  
23 product that isn't stamped -- meaning other tobacco  
24 products -- into the system.

25 Um, you know, arguably, you'll have logs; but  
26 logs are only as good as -- as the people filling them  
27 out, particularly when unless -- unless the  
28 investigators are onsite the day the product leaves one

1 site and goes to the other. Otherwise, um, you could  
2 conceivably have somebody that holds illegal product  
3 in -- in another area and every time that they -- they  
4 sell some of the product down, they just keep refilling  
5 it.

6 And, in most cases, when they blend product  
7 like that, they're also not reporting those sales which  
8 means that there's probably revenue loss on sales tax,  
9 too.

10 Um, when we wrote -- or when we supported AB  
11 71, we probably didn't do as good a job in this area as  
12 far as writing a strict enough portion. But I will  
13 remind you all that what we were -- what we've proposed  
14 as the proponents were to try to get as close to the  
15 good work that the ABC -- or Alcohol has done in this,  
16 where they have very strict rules of transfer of  
17 product. And in that case, a retailer does not have the  
18 right to move their product from one store to the next.  
19 They have to go through the -- the proper channels. The  
20 reason for that -- and -- and alcohol has a much lesser  
21 evasion rate than we have currently on tobacco. Uh, and  
22 they don't have stamps, so it doesn't always mean just  
23 indicia.

24 So, with that, we would support item two. We  
25 would never presume to send in language to the Board on  
26 how to write that regulation because we think that the  
27 staff should write regulations that easily -- that are  
28 easiest for them to -- to enforce than for us.

1 But -- but we believe that the spirit of option  
2 two is closer to what we think would be a better way of  
3 assuring that there's not evasion.

4 Thank you.

5 MS. YEE: Thank you, Mr. Loper.

6 Next, please.

7 ---oOo---

8 STEVEN K. ALARI

9 ---oOo---

10 MR. ALARI: Yes. Good afternoon. My name --  
11 Members of the Board, Madam Chair. My name is Steven  
12 Alari. I'm representing SEIU Local 1000 which  
13 represents the investigators and the, uh, inspectors who  
14 conduct the, uh, inspections.

15 I want to thank staff and the, uh -- and the  
16 Board for sending this back for further revision. I  
17 believe the revisions make it stronger, uh, the  
18 regulation stronger, and we have a letter which is  
19 included Exhibit 4 from our president, Yvonne Walker,  
20 removing our concerns regarding the proposed regulation.

21 Thank you.

22 MS. YEE: Thank you.

23 Let me ask staff, can you address Mr. Loper's  
24 concern with respect to how, uh -- what -- what are the  
25 safeguards against facilitating the transfer of  
26 unstamped products as we allow for this type of transfer  
27 between store locations?

28 MR. BISHOP: Well, the products in question

1 are typically unstamped tobacco products as opposed to  
2 cigarettes. And the safeguards we tried to put into the  
3 regulation deal with inventory control. And that log is  
4 in essence to assist in that aspect, the inventory  
5 control aspect.

6 So any product on the shelf should have an  
7 invoice supporting it. And if that invoice is not  
8 referenced to that particular license location, it would  
9 have to have been transferred and included on that log.

10 It provides the retailer the ability to move  
11 that product around if need -- if need be. And it also  
12 allows for ID, it gives them the ability to at least  
13 verify that that inventory on the shelf is supported by  
14 an invoice and/or the transfer log.

15 MS. YEE: Okay.

16 MR. BISHOP: And it has to be maintained at the  
17 site, and it needs to be made, um -- presented to the  
18 investigator or inspector at the time of the inspection.  
19 So something after the fact would not be accepted.

20 MS. YEE: Mm-hmm.

21 MR. BISHOP: And that product would be  
22 seized.

23 MS. YEE: Okay. And, Mr. Loper, would you  
24 agree that the problem or the potential problem does  
25 mainly affect unstamped tobacco products? I mean we  
26 have a --

27 MR. LOPER: Yeah, I would. But, interesting,  
28 yesterday I think that all of you saw a story in the

1 Sacramento Bee that -- that, um, said in a University of  
2 Michigan study that California's still highly -- have  
3 a -- have a cigarette evasion problem, too.

4 So that seems to me to speak to -- to -- to we  
5 need to take another look at -- at how our enforcement's  
6 going.

7 I mean, I'm particularly proud of Mr. Horton's  
8 bill and particularly proud that the bill has done as  
9 well as it has. But, clearly, there seems to be some  
10 more things happening. We're convinced that OTP, um,  
11 evasion is -- is higher now than it has ever been. And,  
12 um -- and, you know, we -- we appreciate that the staff,  
13 uh, thinks that this is the best method for them to  
14 allow transfers. We just think that the transfers  
15 themselves have inherent problems and allow for ways to  
16 get around it.

17 And, frankly, the staff doesn't know if a can  
18 of Skoal or a roll of Skoal is the same roll that's on  
19 the invoice. They only know the number of pieces of  
20 product that are sold. So there -- there -- you know,  
21 there isn't a way to say for sure that it is that roll.  
22 You can look at the date, but the date on the roll and  
23 the date of the invoice are not going to be the same  
24 thing because the date on the roll is the day that it  
25 was received by the distributor, not the day that it was  
26 sold.

27 So, there are a number of different things, a  
28 number of products that -- that don't even have dating.

1 So I would argue that as much as -- as, you know, this  
2 is -- I will have customers, my client's customers that  
3 will be unhappy with our position. But our position is  
4 not one that we're -- that we're -- you know, we're  
5 wavering on. We believe strongly that there will be  
6 evasion problems and it -- and it will encourage those  
7 people that are -- that are now skirting the law. It  
8 will make it easier and help them to skirt.

9 And -- and, you know, it's not the Safeways of  
10 the world we're worried about. It's the -- the street  
11 operators that concern us.

12 MS. YEE: Sure.

13 MR. LOPER: And it's not the -- the high-grade  
14 tobacconists that we're worried about. It's -- it's  
15 those street operations that -- that have a majority of  
16 the OTP sales in the state.

17 MS. YEE: Mm-hmm. Okay. Uh, thank you, Mr.  
18 Loper.

19 I think, um -- and I do want to hear from the  
20 other Members. We -- we definitely have an issue with  
21 respect to, um, OTP as we continue to have.

22 Uh, I would say that, uh, given the number of  
23 cases that we've seen before this Board where, uh, in  
24 practice, these transfers do occur fairly frequently,  
25 that, uh, this may not be the most, uh -- uh, failsafe,  
26 you know, method of -- of tracking these transfers. But  
27 we at least need to have something that, uh, allows us  
28 to understand what's going on when these transfers do

1 occur.

2           So -- but I would agree with you, more work  
3 needs to be done. We're going to continue to have  
4 evasion and, uh, I'm not sure if this adds to it or  
5 exacerbates it, or, uh -- it probably is a combination  
6 of both.

7           MR. LOPER: I -- I -- I would suggest, Ms. Yee,  
8 that a bright line saying that you can't do the transfer  
9 would have a better impact than one that allows for the  
10 transfer and allows for the -- the -- those that have  
11 been -- been pushing the envelope, gives them more  
12 latitude on how to push the envelope.

13           So I would argue that option two which is a  
14 bright line that says you can no longer do this would --  
15 would also be a stronger way of -- of -- of dealing with  
16 this program.

17           MS. YEE: Okay, thank you.

18           Members?

19           Senator Runner?

20           MR. RUNNER: Yeah, I mean, I think the  
21 challenge we have -- and this is in response to the  
22 issues that we've had before us, you know, with -- with  
23 and -- and ringing our hands over this concept of  
24 transfers, how do you keep track of, what are they  
25 supposed to keep track of, the fact that we ended up  
26 with people with -- without, um, good record, uh, or  
27 historical record as to what -- when -- what was  
28 transferred, certainly not tying it back to inventory or



1     tying it back to invoice, um, was -- was very  
2     problematic. And, you know, as a result of that, we  
3     asked for the interested parties to move forward and try  
4     to come up with -- with -- with -- with solution at that  
5     point.

6             And, you know, I hear the fact that maybe a  
7     bright line is the easiest issue. The problem I have  
8     with the issue of the bright line is it basically then  
9     puts then the -- the -- the, uh, retailer, who are all  
10    very different out there, in the issue of having to then  
11    potentially increase inventory. Because if you've got  
12    to go ahead and you can't split, that means you've got  
13    to go ahead and duplicate inventory.

14            And I think that's, in this day and age, and  
15    asking then inven -- you know, asking a businessman to  
16    increase inventory in order to compensate for the fact  
17    that you can't transfer to me is the hurdle that I have.

18            Um, you know, I think what we need to do is  
19    make sure that whatever we do have in place, and if it's  
20    tying the date back to the inventory, making sure that's  
21    the real record, that we stay as strict to that as we  
22    can and see if it works. If it doesn't work, then we  
23    need to come back and address it. If we see  
24    opportunities for more evasion, then we need to address  
25    it.

26            Um, my concern right now is we're more open to  
27    evasion the way our current system is than we -- than --  
28    than what we're trying to put into place. But, again,

1 I -- I -- in thinking through this, my concern is just  
2 the issue that it puts back on the small operator who's  
3 got to figure out how to move a little bit of inventory  
4 from one place to another, and all of a sudden the only  
5 way to do that with a bright line is through increased  
6 inventory, increased product on -- on the, uh -- on the  
7 shelf.

8 And so, I -- at this point that's why I feel  
9 like at least it's an issue to try and see what works.

10 MS. YEE: Thank you, Senator Runner.

11 Mr. Horton, please.

12 MR. HORTON: Thank you, Madam Chair.

13 Um, you know, as a legislator, we always have  
14 had concerns about legislating to the exception and not  
15 the rule.

16 Um, in this case, most of the audits that we  
17 conduct, uh, there is some indication -- what causes us  
18 to conduct those audits or those investigations, there's  
19 some indication of potential illegal activity. So  
20 wherein the times the Board of Equalization is actually  
21 in these facilities, there's a anticipation that  
22 something may have gone awry.

23 And so the -- the rule may very well be, uh,  
24 more the exception, if you know what I mean.

25 And so, it -- it -- you know, it -- I've gone  
26 backwards and forward on this, um, and took a look at  
27 the, uh, normal business practices. And in the normal  
28 business practice of a large retailer, they're going to

1 have extremely tight internal controls. Uh, and so that  
2 although the blending, you know, is -- is possible, but  
3 the tightening internal controls certainly minimizes  
4 that.

5 Uh, to that end, uh, when -- when a retailer  
6 purchases in bulk, typically, uh, the logic behind it is  
7 to be able to purchase a product at a lower price. It's  
8 not that the merchandise has to go to one location  
9 versus the other.

10 Uh, and so, I'm having somewhat of a quandary  
11 of understanding why there should be transfers,  
12 significant transfers anyway. Uh, and that if they're  
13 purchasing the product, they can direct the distributor  
14 to ship it to whichever location they want it shipped  
15 to. Uh, because the inventory challenges that they have  
16 at one location, theoretically, is going to exist at the  
17 other location. Unless, in fact, they're warehousing  
18 the merchandise; and given the life of this particular  
19 merchandise, that's not happening. I mean, the life of  
20 this merchandise is relatively short. And so, you want  
21 to get it from the distributor to the customer as soon  
22 as possible.

23 So, um -- I would -- I would add to the  
24 requirement that in purchasing, whenever you're  
25 purchasing in bulk, that the distributor has to ship it  
26 to the specific location and that any transfers between  
27 these should be incidental and nominal, and so that you  
28 don't see these major transfers, which is where -- which

1 lends itself to -- to, uh -- to the blending concern.

2 Um, and I don't know what that incidental  
3 number might be. I don't know if it's cartons. I don't  
4 know if it's cases. Uh, but I do know that, uh, the  
5 industry practice -- I mean, if you look at your major  
6 stores, they're shipping the merchandise directly to the  
7 store based on their sales volume. And a retailer in  
8 his -- his mode of business, mode of operation is going  
9 to make that assessment. This store will sell, on  
10 average, X amount, therefore I'm going to purchase on  
11 average, so forth.

12 So unless there is some, uh -- and I would go  
13 to the, uh -- to the industry. Unless there is some  
14 prohibition from the distributor actually shipping it to  
15 the -- the place of potential sale, then there shouldn't  
16 be a whole lot of transfers anyway. And if there are,  
17 they should be incidental.

18 MR. LOPER: If I -- if I may. Um, we can -- we  
19 can deliver to whatever location the -- the person --  
20 the retailer or the purchaser wants. Um, and if -- and  
21 if a retailer buys at Costco or they do their own  
22 delivery, they have the right also to -- to separate the  
23 invoices at the time of sale for each location.

24 Now, I would remind the Board that in the case  
25 of alcohol, there is not that right to transfer product.

26 MR. HORTON: It's prohibited.

27 MR. LOPER: And -- and -- and it's specifically  
28 prohibited. The error that -- that -- you know, and

1 maybe it's in need for legislation is, is that maybe it  
2 needs to be specifically prohibited in this case, too.  
3 Because in the -- if the retailer knows what their --  
4 what their store is doing, they shouldn't be  
5 over-ordering in one and not in another.

6 And on that occasion it will happen,  
7 Mr. Runner. But for the most part I would argue that  
8 most stores that are well-managed know the difference  
9 and they don't do it in alcohol. And it's -- and we're  
10 talking about these stores are basically all the same  
11 kind of stores. They -- they -- they manage their  
12 inventories in the same way. And there's a reason why  
13 they don't -- that -- that alcohol has -- has kept it  
14 this way. Um, and I -- I think that -- that it would be  
15 a stronger way to protect the -- the taxpayer.

16 Now, you know, I'm -- I'm interested in people  
17 that operate legally. And people that operate -- and it  
18 is too bad that we have to -- to regulate to protect  
19 those people. But in this case I think the regulation  
20 should be a bright line.

21 And, um, I'm -- I'm sorry, I can't be convinced  
22 that this regulation is going to -- is going to help  
23 and -- and that is the reason why we've opposed it.  
24 It's not because we're -- we're -- we want to make it  
25 harder on our customers. It's because we believe  
26 strongly that our members and our good customers will  
27 be -- will be eventually harmed.

28 MR. HORTON: Uh, Mr. Loper, I appreciate that.

1           Um, the question before you, um, the liquor  
2 industry, they too purchase in bulk for the purpose  
3 of -- of reducing cost. And they will ship that  
4 merchandise to a particular location.

5           MR. LOPER: They have -- they to have deliver  
6 by location.

7           MR. HORTON: By location.

8           MR. LOPER: By location.

9           MR. HORTON: And so --

10          MR. LOPER: Specific to the statute.

11          MR. HORTON: And so why not do that in this  
12 case? Um, require that the distributor delivers by  
13 location and so the merchandise -- to not take away the  
14 opportunity to purchase in bulk. So that they maintain  
15 the opportunity to purchase in bulk, but the distributor  
16 has to deliver it to, uh, the location and reduce the  
17 amount -- the level of which can be transferred by  
18 virtue of these log-in inventory controls to a nominal  
19 amount in the event that they -- there are some  
20 miscalculations, uh, let's say. I don't -- I'm not  
21 familiar enough with the industry to come up with an  
22 arbitrary number.

23          MR. LOPER: I -- I guess my answer would be --

24          MR. HORTON: But if you allow me to finish.

25          MR. LOPER: I'm sorry.

26          MR. HORTON: The incidental transfer, somewhere  
27 around, uh, you know, \$250, \$500, uh, I mean you're  
28 not -- but the -- the bulk transfers are handled by

1 the -- or the bulk distribution, if you will, is handled  
2 by the -- by the distributor and not by the -- the  
3 retailer. Because I too have some concerns, and I'm  
4 trying to have some flexibility here when you have  
5 incidental transfers that are -- that, in the normal  
6 course of business, couldn't be anticipated.

7 MR. LOPER: Um, if -- maybe. I mean I -- to  
8 help you with where I think you're going, I would say  
9 that the bright line basically answers the first  
10 question, because then we have to be -- then the product  
11 has to be specific to each location.

12 But, having said that, if -- if you're going to  
13 this issue of how do you accommodate those emergency  
14 situations, perhaps you'd put a limit on the number of  
15 times per calendar year a store can do those, and  
16 that -- and that they have to notify the Board at the  
17 time that they're making those transfers.

18 I mean, perhaps that would -- would strengthen  
19 the -- the spirit of what you're trying to do, um, and  
20 would get to Mr. Runner's issues, or perhaps Ms. Steel's  
21 issues. But -- but I -- if -- if -- if there's a need  
22 to figure out a way to do this because there's this --  
23 this -- of this issue, then I would argue perhaps you  
24 limit the number of times those transfers can be made,  
25 and perhaps you do that upon some sort of notice to the  
26 BO -- to the Board to either ID or to the excise unit at  
27 the time that the transfer's going to be made. So that  
28 the line becomes brighter. That people don't just

1 say -- just don't fill in logs and -- and, you know, do  
2 what they -- they want to do without having some  
3 controls, stronger than just the ID's logs that they've  
4 suggested.

5 MR. RUNNER: Madam Chair.

6 MR. HORTON: Uh, Members, I mean, we -- we --  
7 here's -- here's our challenge, in my mind, is that last  
8 year we audited some 10,000 different, uh, retailers,  
9 somewhere around there, I believe. Strike that.

10 I'm -- I'm referring to the annual report in  
11 2007, which is some time ago. Um, at that time we were  
12 somewhat at the peak of our activity, uh, and not as  
13 proficient as we are now.

14 MR. ALARI: 2004.

15 MR. HORTON: Our team is extremely more  
16 proficient. Uh, and we're not looking at that  
17 significant number of inspections anymore.

18 But then, of those inspections, a nominal  
19 amount actually yielded; I believe, the amount, if I  
20 remember correctly, was \$16 billion.

21 Since then, this program has generated  
22 hundreds -- a little over -- over hundreds of millions  
23 of dollars. I don't know the exact numbers, but I'll  
24 give you the credit anyway. Um, and so we're more  
25 focused than we've ever been before on our inspections.

26 And I, for one, think the criminal element in  
27 the State of California is on a rise; that the  
28 underground economy, the, uh -- the, uh, organized crime



1 is engaging in the distribution of counterfeit products  
2 at every level. And -- and we don't have enough force  
3 to -- to really deal with that issue.

4 But at the same time, I don't want to be  
5 punitive of a business that, uh, we may never audit, we  
6 may never suspect. But they're going to do what they  
7 can to adhere to the law, uh, and thereby when those  
8 incidental transactions do occur, we should be able  
9 to -- to -- to -- to -- to -- to accommodate that.

10 But there should be some -- it just seems to be  
11 counterintuitive that a retailer has to inventory large  
12 amounts of cigarettes and then distribute them from  
13 their location, uh, when it's more convenient to have  
14 the distributor distribute -- distribute it based on  
15 your sales volume, per location, and then make those  
16 minor adjustments whenever we need to, so we allow for  
17 those minor adjustments.

18 Thank you, Madam Chair.

19 MS. YEE: Thank you, Mr. Horton.

20 Senator Runner, please.

21 MR. RUNNER: Yeah, yeah. I guess my -- my  
22 thought is that these are incidental. And so maybe, um,  
23 that we're not intending this to be mass transfers of  
24 lots of product back and forth.

25 So -- so I really don't have an issue in  
26 regards to creating some kind of cap or something that  
27 would -- that would limit it in some way. Because it  
28 seems to me that, again, my concern is just that all of

1 a sudden some product -- a little bit of product needs  
2 to be moved over there, then there's a process to do  
3 that. Certainly not trying to bring everything into a  
4 warehouse to be distributed then amongst two different  
5 stores or something like that. And if -- and if that's  
6 what this opens up, I certainly think that's  
7 problematic.

8 So, um -- but, again, I think the incidental  
9 movement is certainly something that in the normal  
10 course of business somebody would clearly get in the  
11 middle of and need to do.

12 Um, I -- I'm probably, again, uh, I'm not sure  
13 how much of this kind of a discussion happened in the  
14 interest parties meeting discussions, and so, you know,  
15 if these were part of the topics.

16 I'm not sure I -- I -- I'm concerned about the  
17 fact that somebody would be contacting the BOE every  
18 time there was a transfer. That sounds like it's, um, a  
19 bit of a -- a bit of a, uh, hassle for not only the,  
20 uh -- the, uh -- the retailer, but also then for -- for  
21 inventorying that and keeping track of that for the --  
22 for the BOE.

23 Um, but certainly I think there can be some  
24 limits on that. And it's certainly not my thought or  
25 intention that this be unlimited transfers and the  
26 ability then to -- it would -- it would be a perversion  
27 of -- I think what we were trying to do, if all of a  
28 sudden this became a way to, um, you know, bring

1 something into one place and then sort it out to four  
2 different places and, um -- as opposed to just saying,  
3 hey, I ran out of cartons of this or I ran out of, you  
4 know, tins of this and I need to put some over in that  
5 other store.

6 Um, that's what I -- at least those are the  
7 ones that have come before us. And so that's kind of  
8 what my thinking was because that was the nature of what  
9 was coming before us.

10 MS. YEE: Yeah.

11 MR. RUNNER: So --

12 MS. YEE: Let me -- let me, uh, just direct  
13 this question back to the staff then. Two -- two  
14 thoughts: One, in response to Senator Runner's comment  
15 just now. Um, I mean, I think what we were  
16 contemplating was really the situations that were before  
17 this Board with respect to, uh, really the more  
18 incidental (inaudible) and transfers.

19 MR. BISHOP: Correct, that's our current  
20 policy. The current policy was drafted after seeing a  
21 number of smaller retailers that had a couple of  
22 locations that were moving, you know, a couple hundred  
23 dollars worth of product at any given time --

24 MS. YEE: Mm-hmm.

25 MR. BISHOP: -- and not having, uh, transfer  
26 logs prepared in advance.

27 MS. YEE: Uh-huh.

28 MR. BISHOP: So being in situation of how do we

1 handle that. And so staff promulgated, well, put  
2 together the policy and then circulated that to all the  
3 retailers with multiple locations that are selling  
4 cigarettes or tobacco products, and it was approximately  
5 1700.

6 So, we felt that we needed a regulation so  
7 that, as these situations come before you, you have  
8 clear -- one, the retailer has clear guidelines on what  
9 they need to do, and the Board has a regulation that it  
10 can point to in support.

11 The Act, in my review of the Act, does not  
12 require that items be sold from the store in which they  
13 are delivered to. That is -- that is not -- ABC  
14 statutes are not replicated here in that situation.

15 So there is a -- regardless of what the Board  
16 decides, if we go with short -- allowing transfers, the  
17 Act provides for it. If we say it has to be sold from  
18 the location in which the store that it was delivered  
19 to, that would require a regulation because the Act is  
20 not -- it does not state that.

21 And I think if you want to limit the ability of  
22 a retailer, a legitimate retailer from moving product  
23 from one location to another, you need to be very clear  
24 within either the Act or within a regulation, because  
25 otherwise we're in the same quandary we're in today,  
26 that we're trying to get clarity on these transfers.

27 But some of the retailers that I've dealt with  
28 that are smaller, that have -- that are presum --

1     ostensibly legitimate, they purchase at one location.  
2     They're small, you know, one-person-owned location or  
3     business and they want to control that inventory. So  
4     they want to take delivery at the location that they're  
5     physically at and then they move it to their other  
6     store.

7             So that is occurring with, um --

8             MR. HORTON: Yeah.

9             MR. BISHOP: -- the gentleman that was at the  
10    interested parties meeting. And that -- his concern is  
11    this would put him out of business if we were to not  
12    allow for transfers. And -- and again, he buys in bulk  
13    and I believe if he was having it delivered to different  
14    locations, he may be able to get a discount in terms of  
15    the product discount in terms of the bulk, but is he  
16    going to get hit with delivery charge? And then if he's  
17    not physically at that location taking delivery, one of  
18    his employees is doing it. And so he would prefer that  
19    he is able to take control of that product himself.

20            Now --

21            MR. LOPER: If I remember right, that was a  
22    licensed distributor.

23            MR. BISHOP: He happens to be, yes.

24            MS. YEE: A licensed distributor?

25            MR. BISHOP: So he would have to invoice to  
26    himself then.

27            MS. YEE: Mm-hmm. Right, right.

28            Mr. Horton.

1 MR. HORTON: You know --

2 MR. BISHOP: And it's a thousand dollar monthly  
3 or annual fee.

4 MS. YEE: Right.

5 MR. HORTON: A small retailer doesn't have  
6 multiple locations that they have to distribute to.  
7 That, in and of itself, is counterintuitive, not  
8 definitive of a small local retailer. Uh, so that  
9 argument seems to, uh -- doesn't seem -- and I know  
10 you're just delivering the argument.

11 MR. BISHOP: Right.

12 MR. HORTON: But it just seems to be  
13 inconsistent.

14 And, uh -- and then there's a presumed distrust  
15 among his -- his other distributors. They don't -- they  
16 don't trust them for the same reason that we have  
17 challenges with blending. They, too, can be blending on  
18 him so that he -- if he's not controlling the industry,  
19 his -- one of his retail outlets could be moving illegal  
20 product in there and his product never getting sold but  
21 the illegal product's getting sold. And so he's got his  
22 own operation set up.

23 So he has the same concern. And that's  
24 indicative of the problem that we're trying to address.  
25 And -- and, uh, given the, uh -- you know, the evasion  
26 problem here and given the fact that we're focusing  
27 on -- we're far more focused than we've ever been before  
28 in our investigation that we're not auditing the average

1 Mom-and-Pop operation out there that, by all  
2 appearances, seem to be doing it right. Uh, we have  
3 more extensive investigation, uh, capacity now. And  
4 we're a little more focused.

5 So, that still does not seem to justify the  
6 transfer of anything more than what you've articulated,  
7 uh, \$200 incidental that may occur on a quarterly basis  
8 to make an adjustment for, uh, a miscalculation in  
9 sales, sales volume, something of that nature.

10 And so, a combination of a bright line test  
11 that allows for, uh -- that requires the distributor to  
12 ship directly to the -- to the point of sale, uh, or  
13 anticipated point of sale, with some minor incidental  
14 ability that it, too, has inventory control.

15 I'm not necessarily thinking that taxpayers  
16 ought to be reporting their transfer of inventory to the  
17 Board of Equalization. But there should be onsite  
18 inventory records, and they should keep the normal  
19 inventory records that the vendor that you described is  
20 probably keeping; uh, inventory control, quarterly  
21 inventory, independent inventory, you know, all of that,  
22 uh, should be maintained, not because the Board requires  
23 it, so -- but because it's normal business practice to  
24 control this volatile -- this particular industry that  
25 has these challenges.

26 MR. ALARI: One -- one -- one point.

27 MR. HORTON: Member Yee?

28 MR. ALARI: Ms. Yee, I'm sorry.

1 MS. YEE: Sure. Let me have Mr. Loper, Mr.  
2 Alari, respond briefly. And then, uh --

3 MR. LOPER: I -- I -- I guess I would point out  
4 and maybe Mr. Alari was going to point out, this  
5 regulation is not an incidental regulation. It  
6 doesn't -- it doesn't address this as an incidental  
7 action. It allows for actions on a daily basis --

8 MR. HORTON: Right.

9 MR. LOPER: -- as actually outlined by staff.

10 MS. YEE: Mr. Alari.

11 MR. ALARI: Yeah, Member Chair, to the point,  
12 uh, Mr. Horton -- Board Member Horton had said, we're  
13 having our annual meeting right now. And we just gave  
14 our report; for 2011-2012, our members have inspected  
15 approximately 10,400 in that period.

16 And, uh, one of the reasons that SEIU has -- is  
17 not opposing this regulation -- it's withdrawn -- is  
18 because in the additional language that was added in is  
19 that we are going to be asking for transfer documents  
20 commencing -- when we commence our inspections, and they  
21 cannot create them or give them to them afterwards.

22 We think that that will be helpful when we  
23 conduct these inspections. That additional language, we  
24 think it's very important.

25 MS. YEE: Okay.

26 MR. BISHOP: And I will add that blending can  
27 occur within a single location. Multiple locations --  
28 it's not necessary to have more than one location to



1     blend.

2             And what staff was trying to do, again, was to  
3     put in regulation form the current policy of the Board  
4     and the practice in the industry, albeit on a limited  
5     basis, but it does give the latitude to those retailers  
6     to transfer product of a -- of a type that is going to  
7     go bad after a period of time. So -- which is different  
8     than alcohol. Alcohol's not going to spoil, but the  
9     snuff or the cigars will eventually go bad if not  
10    properly humidified.

11            So, they're able to move that product, again  
12    legitimately, between locations where the sale may take  
13    place and so they can sell the product before it does go  
14    bad, before they have to return it to their distributor.

15            And this is -- we saw this as a business --  
16    retail -- retail business friendly proposal.

17            MR. SMITH: In staff's view, um, this  
18    regulation would not increase evasion because the  
19    transfer logs would have to be at the store at the time  
20    the inspector arrives.

21            After -- this would tighten current practice  
22    really, because currently some retailers attempt to  
23    provide transfer logs after the fact, and that becomes a  
24    contentious issue for us.

25            But I think this would clarify that all the  
26    records have to be in place at the time the inspector  
27    arrives.

28            MS. YEE: Okay. Very well.

1 Other comments, Members?

2 Hearing none, is there a motion?

3 MR. HORTON: Yeah, um, I would move that we  
4 limit the transfers to the \$200 a quarter, uh, and  
5 require the inventory, um -- all of the inventory  
6 controls, including the transfer log, um, and that there  
7 are no exceptions once the auditor's onsite. And  
8 anything in excess of that should be delivered by the  
9 distributor and not -- so we should have a bright line  
10 test that prohibits any excess transfers between stores,  
11 period.

12 But with that, Members, the concern is is that  
13 the law -- I mean, this is -- this is -- this is -- this  
14 is what books and records look like, whatever you write  
15 down on a blank sheet of paper. And so that can -- that  
16 can certainly be of a concern, uh, is of a concern for  
17 me and can -- tied in with the whole evasion thing.

18 And I -- I respectfully disagree, uh, with  
19 staff and would remind staff that when we were going  
20 through the process with AB 71, identified this as a  
21 huge problem. Staff didn't agree at that time either,  
22 but we've subsequently proven that it is just a major,  
23 major problem for the State of California. And we don't  
24 want to open any doors, uh, that we have to -- that may  
25 be of a challenge later on.

26 The other concern is that these -- these  
27 cigarettes are being sold to kids, and they're being  
28 sold illegally. Uh, the funding, excess funding is

1 being used for other criminal activities. I mean, this  
2 is a -- this is a huge problem.

3 When we were going through the process of  
4 debating the legislation, it was discovered that the  
5 revenue from this was being used to fund terrorist  
6 activity, uh, against the United States. And we were  
7 able to shut that down. The investigations that have  
8 yielded significant, uh, disclosure of unreported  
9 taxable sales, we found human trafficking existing, uh,  
10 as a result of perpetuating this illegal activity.

11 So, it's a -- it's a much larger concern than  
12 just a retailer being able to transfer. But I do want  
13 to accommodate them. And I think that nominal amount  
14 somehow -- whatever that number might be. I hate to  
15 speak on behalf of the small retailers out there, what  
16 their needs are.

17 But your own testimony, uh, staff's testimony  
18 was \$200. And based on your testimony, uh, pursuant to  
19 what you've heard from staff, I believe it was actually  
20 \$200 a quarter or something like that, but -- so that  
21 would be my motion. If you can -- that was a long  
22 motion.

23 MS. YEE: Okay. We have a motion by Mr. Horton  
24 to, uh, limit the application of, uh, the transfer to  
25 \$200 a quarter, keeping the inventory control  
26 requirements as proposed in place, and that the, uh --  
27 any amounts in excess of that would be, uh, subject to,  
28 uh, distribution to locations by distributor.

1 MR. HORTON: Yes.

2 MS. YEE: Okay. Is there a second?

3 I want to give it a courtesy second for  
4 discussion.

5 MR. RUNNER: Okay.

6 MS. YEE: I, um -- I feel like we need -- we  
7 need a measure in place now to deal with -- I'm sure  
8 there are going to be more cases that we're going to  
9 hear before we get something in place. So I do think  
10 there's some sense of urgency to this.

11 Um, and I think the staff has done, uh, good  
12 work in terms of outreach to the parties that would be  
13 affected. And, Mr. Chairman, on your proposal, um,  
14 would that change? I feel like I'd like to see it  
15 developed -- re -- reformulated and have it come back to  
16 the Board.

17 Um, there's a lot in that. I think the  
18 outreach that we would do around that is different from  
19 what the staff has already done. And, uh, I'd just like  
20 to kind of see it in whole again.

21 MR. HORTON: Yeah, I -- I -- I would agree with  
22 that, Madam Chair. I mean, if we send it back to staff,  
23 there's enough history here, uh, where we've had these  
24 problems. And to actually come up with numbers, as I  
25 indicated, I don't necessarily want to impose --

26 MS. YEE: Yeah.

27 MR. HORTON: -- an arbitrary number, uh, and  
28 just wanted to, uh, philosophically sort of delineate

1 the two efforts here.

2 MS. YEE: Okay. Um, I also think every time we  
3 speak about any change in this particular area of our,  
4 uh, administration of this particular tax area, that  
5 there are multiple objectives that we're trying to  
6 accomplish when we put these regulations in place. And  
7 some of which I don't think necessarily are on-point  
8 with respect to the -- the -- the focus at hand.

9 So, uh, I want to be mindful of that and not  
10 lose sight of kind of the origin of the concern with  
11 respect to what this regulation was trying to respond  
12 to.

13 So, uh, I would like to see this come back.  
14 But other, uh, thoughts, Members?

15 MS. STEEL: I --

16 MR. HORTON: Ms. Steel, then Mr. Runner.

17 MS. STEEL: I want staff to work on the numbers  
18 because 200 number -- \$200 is too arbitrary here for a  
19 quarter.

20 And I know Mr. Loper thinks that I'm very much  
21 sympathetic to small business owners. This one is, you  
22 know -- I'm talking about few dollars that they transfer  
23 and they get penalized and they have to close for ten  
24 days. When, you know, you're looking at those small  
25 stores, to ask them to close -- I mean, you know, make  
26 them to close it for ten days means that they have to  
27 close down for whole store.

28 So I really want staff to come back with the

1 numbers for the average, because I see a lot of small  
2 numbers, but \$200, I -- I really want to figure out  
3 that, you know, what number is the really better number  
4 here. Because I think Chairman Horton just came out  
5 from -- just 200 from, you know --

6 MR. HORTON: Out of the sky.

7 MS. STEEL: Yeah. Exactly. He just picked it.  
8 So I want something to --

9 MR. RUNNER: Limited research.

10 MS. STEEL: -- reasonable that -- that, you  
11 know, uh, not making small stores, they to have close  
12 down because of these penalties.

13 So, you know, I -- I just really want to see a  
14 little more flexible. I totally understand your point  
15 of view because everything has to be very strict, so  
16 most of the industries that they are doing honest  
17 businesses that they have to survive.

18 But at the same time, some of these small  
19 businesses, when they own couple of stores or they have  
20 their friends and they want to borrow just a little bit,  
21 it has to be little flexible here. But I don't like  
22 that 200 number. So let's, uh, you know, ask staff to  
23 come back that what's the best number to work with and  
24 then, you know, I want to see it.

25 MS. YEE: Okay.

26 MS. STEEL: Yeah.

27 MS. YEE: Senator Runner.

28 MR. RUNNER: Yeah, I -- I -- like I said, I

1 think we can find something that will work. I -- I just  
2 get concerned that we would be up here making up a  
3 number. We've had a, uh, interested parties in place.  
4 And, um --

5 MR. HORTON: "Ditto" will suffice.

6 MR. RUNNER: And -- and, uh -- and I think it's  
7 good to hear back from, uh, those groups to say what  
8 that would work with, with the impact. Because I'm not  
9 sure if there was ever a consideration during that  
10 interested parties about -- I mean, I think it was  
11 either of transferring or not transferring. I think --  
12 I don't know if they -- they ever got the discussion of  
13 limiting transfers, and that's a different kind of  
14 discussion. And I think before we do that, we need to  
15 let the process take care of it.

16 MS. YEE: Okay.

17 Mr. Horton, do you want to just, uh, change  
18 your motion to direct it to the staff?

19 MR. HORTON: I withdraw the motion and yield to  
20 your direction, Madam Chair.

21 MS. YEE: Okay. Um, why don't we have the  
22 staff then, uh, hearing the concerns that have been  
23 expressed today, we are looking at, uh, limiting the  
24 application of, uh -- well, limiting transfers and what  
25 that may look like.

26 Perhaps start with the proposal that was put on  
27 the table and, uh, certainly from an administration  
28 standpoint from the small business perspective impact,

1 uh, retailer impact, and, uh, also the distributor  
2 impact with respect to what we do with, uh, those, uh,  
3 amounts beyond any limitation we impose.

4 Okay. And, uh, I would like -- we did go  
5 through an interested parties process, uh, on this. I  
6 would like to be sure that all the interested parties  
7 are kept aware of the developments of our discussion  
8 here.

9 MS. BUEHLER: Certainly.

10 MS. YEE: And, uh, we'll work with you on that  
11 time frame for bringing this back.

12 MS. BUEHLER: Thank you.

13 MS. YEE: Okay. Without, objection, that will  
14 be the direction. Thank you.

15 MR. LOPER: Thank you.

16 MS. YEE: Thank you.

17 ---oOo---



1 ---o0o---

2 MS. YEE: All right. Our next item, Members,  
3 is proposed amendments to Regulation 1685.5, a  
4 Calculation of the Estimated Use Tax, using the use tax  
5 table.

6 We have one speaker on this item, Miss Gina  
7 Rodriquez, if you'll come forward.

8 And we'll have the staff introduce the issue.

9 MS. BUEHLER: We actually have one more action  
10 item still under the --

11 MS. YEE: Oh, I'm sorry.

12 MS. BUEHLER: -- Cigarette and Tobacco.

13 MS. YEE: We do?

14 MS. BUEHLER: We do.

15 MS. YEE: Oh, was it the other amendments?

16 MS. BUEHLER: Yes.

17 MS. YEE: Okay. I'm sorry.

18 MS. BUEHLER: That's all right.

19 MS. YEE: Let me, uhmm, move back to item 1  
20 then.

21 So, we have given staff direction with respect  
22 to revising or further modifying Regulation 4801. It  
23 looks like we also have then the requirement of Board  
24 adoption to publish amendments to Regulations 4601 and  
25 4603, 4604 and 4605.

26 And this relates to -- to allowing any notice  
27 under the Cigarette and Tobacco Products Licensing Act  
28 to be served personally or by mail and to allow reduced

1 suspension period of five days, which is in addition to  
2 the already allowed zero, ten and twenty days with these  
3 respective regulations.

4 Okay.

5 MR. HORTON: Move adoption.

6 MS. YEE: Okay.

7 Moved by --

8 MS. MANDEL: I didn't even see that in the  
9 issues.

10 MR. BISHOP: It's in the agenda.

11 MS. YEE: Okay. Moved by Mr. Horton.

12 Is there a second?

13 MS. MANDEL: Oh, that's from before.

14 MS. YEE: Yes, uh-huh.

15 MR. RUNNER: Correct.

16 MS. MANDEL: Oh, okay, sorry.

17 MS. YEE: Okay, motion by Mr. Horton to adopt  
18 those amendments.

19 Second?

20 MS. STEEL: I second that but I wanted staff to  
21 come back, maybe year from now, that, you know, how many  
22 people are getting from zero to five days.

23 I'm very much concerned that small business  
24 owners, instead of getting zero now, there is between  
25 zero to ten. So, I want to see the numbers of five days  
26 to -- they supposed to get zero, but they get five  
27 days.

28 MS. YEE: Okay.

1 MS. STEEL: Thank you.

2 MS. YEE: You're welcome.

3 Motion by Mr. Horton, second by Ms. Steel, with  
4 a request by staff to provide an update after a year on  
5 the impact.

6 Without objection, Members?

7 MS. MANDEL: Yeah, I just had one that --

8 MS. YEE: Are you okay?

9 MS. MANDEL: -- yeah, I'm okay with this. I  
10 had one little note --

11 MS. YEE: Yes.

12 MS. MANDEL: -- on something else.

13 MS. YEE: Do you want to make --

14 MS. MANDEL: Oh, yeah. On -- just on the 4801,  
15 on the legal entity, if it goes forward like that I  
16 think you're going to have to pay -- I mean, I still got  
17 confused because I realized that you're using "legal  
18 entity" to also refer to a natural person and that  
19 that's taken care of by the example that you put.

20 So, I -- since, to me, "legal entity" just  
21 means an actual thing created under the Code somehow, I  
22 was confused and I was trying to think of other ways you  
23 would say -- say it, like, you know, when the licensee  
24 for the retail location, transferring in the licensee,  
25 receiving are the -- are identical.

26 I thought, "Oh, well, for want of a -- for want  
27 of an initial on one of the licenses, you know, the guy  
28 would lose."

1 I was like, "Well, what about if it said the  
2 same?"

3 Well, but then we have the whole argument  
4 about, "I'm really the same."

5 So, I guess maybe that's where you wound up  
6 with legal entity, but I thought there was potential  
7 for -- still just potential for confusion when I  
8 realized that you were using it for -- last meeting I  
9 was focused on, you know, parents, subsidiary and that  
10 kind of thing and that's not what we were talking about.  
11 We were just talking about the exact same legal entity.

12 I hadn't focused that you were using it to also  
13 reference a natural person. So, that --

14 MR. SMITH: Yeah. Well, in the initial draft  
15 it included natural person.

16 MS. MANDEL: Yeah, I just --

17 MR. SMITH: And then in the second draft we  
18 added the parents of example to try to --

19 MS. MANDEL: -- right. Well, I meant that the  
20 phrase "legal entity" itself, that I'm the same legal  
21 entity.

22 MR. SMITH: -- yeah.

23 MS. MANDEL: I mean, I -- you know -- but maybe  
24 I'm sensitive to it because we get these letters from  
25 tax challenged that talk about legal entity.

26 I don't think of myself as a legal entity. So,  
27 that's why I found the language -- I don't know what.

28 MR. SMITH: We had some internal debate about

1 that.

2 Do you think "person" would be better than  
3 "legal entity"?

4 MS. MANDEL: Well, I mean, this is being put  
5 over so maybe we just, you know, talk about it later,  
6 but I -- I know you went through the -- "We don't want  
7 to use 'person' because that's too confusing."

8 But I -- I don't know if everyone in the world,  
9 you know, thinks "legal entity" can include a -- when  
10 they read it -- they'd have to go to the -- they'd go to  
11 the example, which is in the same paragraph that talks  
12 about natural person, but it just -- I guess I hadn't  
13 picked up on that you were using it to mean also a -- a  
14 natural person, since I was so focused last time on the  
15 related corporation-type issue.

16 MR. BISHOP: I think our discussion, in some  
17 sense, when we came up with "legal entity" and there was  
18 a discussion whether it should be "person."

19 The title of the regulation actually has  
20 "person" in it, saying "person." And, so, it alludes to  
21 the person and then it -- we further define that person  
22 as a "legal entity" the same and "Here's some examples  
23 of a type of legal entity" --

24 MS. MANDEL: All right.

25 MR. BISHOP: -- "which would be the same."

26 MS. MANDEL: Okay. You think you've walked it  
27 through? Okay.

28 MS. YEE: Well, take a -- take another look as

1 you're going back and looking at the other --

2 MR. BISHOP: Sure.

3 MS. MANDEL: That was the only note.

4 MS. YEE: -- actual areas for modification.

5 MS. MANDEL: Thank you.

6 MS. YEE: Okay. So, we have motion by  
7 Mr. Horton, second by Ms. Steel with respect to adoption  
8 of the amendments to 4601, 03, 04, 05 and with an update  
9 in a year on its -- on their impact.

10 And without objection those amendments are  
11 adopted and authorized for publication.

12 Thank you.

13 MR. BISHOP: Thank you.

14 MS. YEE: Okay, thank you.

15 Item No. 2, proposed amendments to  
16 Regulation 1685.5 with respect to the use tax table.

17 Ms. Buehler.

18 MS. BUEHLER: For agenda items 2 and 3, Bradley  
19 Heller from our Legal Department is joining me.

20 MS. YEE: Great. Good afternoon, Mr. Heller.

21 MR. HELLER: Good afternoon.

22 MS. BUEHLER: For agenda item 2 we request your  
23 approval and authorization to publish proposed  
24 amendments to Sales and Use Tax Regulation 1685.5,  
25 calculation of estimated use tax, use tax table.

26 Staff's proposed amendments account for the new  
27 registration requirements imposed by Assembly Bill 155  
28 and recent registration activities by changing the

1 estimated percentage of California consumers' total  
2 purchases -- purchases made from out-of-state retailers  
3 that are not registered with the Board to collect use  
4 tax from their customers from 37 percent to 23 percent.

5 The amendments would apply to the 2013 use tax  
6 table, which covers purchases made during the 2013  
7 calendar year.

8 Staff will continue to monitor the  
9 implementation of Assembly Bill 155, registration  
10 activities and other data sources to determine whether  
11 the methodology used to estimate the 23 percent can be  
12 incorporated into Regulation 1685.5 and used on an  
13 annual basis.

14 For the Board's general information, we note  
15 that based on data from the Franchise Tax Board,  
16 participation and the number of taxpayers reporting on  
17 the use tax line of their FTB returns nearly doubled  
18 2011 to 2012, with a revenue increase of \$9.8 million.

19 I believe we have a speaker for this item,  
20 after which we'd be happy to answer any questions you  
21 may have.

22 MS. YEE: Okay. Thank you, Ms. Buehler.

23 Good afternoon, Ms. Rodriquez, thank you for  
24 your patience.

25 ---o0o---

26 GINA RODRIQUEZ

27 ---o0o---

28 MS. Rodriquez: Thank you, Madam Chair and

1 Members and happy new year to all of you.

2 Gina Rodriquez with California Taxpayers  
3 Association. Cal-Tax did participate in the interested  
4 parties meetings and, as a result of staff conducting  
5 these meetings, we feel that taxpayers have been well  
6 served.

7 Staff was very receptive to Cal-Tax's concerns,  
8 specifically with the narrow AGI ranges that were  
9 initially proposed. Those AGI ranges have subsequently  
10 been widened.

11 Also our concern with -- with the lack of  
12 attention to AB 155 and, as Ms. Buehler just stated,  
13 AB 155 has been addressed.

14 They're doing a 14 percent reduction in looking  
15 at consumers' total purchases that are made from  
16 out-of-state online retailers.

17 So, for these reasons, we totally support  
18 staff's request to approve and authorize to publish the  
19 proposed regulation.

20 Thank you.

21 MS. YEE: Thank you very much. And thank you  
22 for your participation.

23 Comments, Members?

24 MR. HORTON: Move adoption.

25 MS. YEE: Okay. A motion by Mr. Horton. Is  
26 there a second?

27 MS. MANDEL: Second.

28 MS. MANDEL: Second by Ms. Mandel.



1 MS. YEE: Senator Runner, do you have a  
2 comment?

3 MR. RUNNER: No.

4 MS. YEE: Okay.

5 MS. STEEL: I have a little comment.

6 MS. YEE: Yes, Ms. Steel.

7 MS. STEEL: I think 23 percent is still too  
8 high, but it's better than 37 percent figure, so, I just  
9 go for it.

10 MS. YEE: Okay, noted.

11 Other comments?

12 Okay, motion by Mr. Horton, second by  
13 Ms. Mandel.

14 Objection?

15 Hearing none the request to approve and  
16 authorize publication of these amendments is adopted.

17 Thank you.

18 And our last item is Regulation 1502, and 1507.  
19 This relates to computers, programs and data processing  
20 and technology transfer agreements.

21 We have several speakers on this issue. Let me  
22 ask them to come forward, please?

23 Mr. Julian Decyk with Paul Hastings, Mr. Mark  
24 Nebergall with SOFTEC, Miss Rodriquez with Cal-Tax and,  
25 I believe, that is it.

26 Please come forward and we'll have Ms. Buehler  
27 and Mr. Heller introduce the issue.

28 MS. BUEHLER: In action 1, regarding whether to

1 amend Regulation 1502, computer programs and data  
2 processing to clarify how sales and use tax applies to  
3 transfers of prewritten software recorded on tangible  
4 storage media, we request your approval to conduct  
5 additional focused interested party meetings on issues  
6 which, based on prior interested party meetings, have  
7 the best potential for immediate resolution.

8           These issues include the application of tax to  
9 optional software maintenance contracts that include the  
10 transfer of a backup copy of the same or similar  
11 prewritten software recorded on tangible storage media  
12 and the application of tax to site licensed  
13 transactions.

14           If approved, we anticipate holding one  
15 interested parties meeting on the first issue to be held  
16 at the beginning of March and two interested parties  
17 meetings on the second issue to be held in April and  
18 June. Staff would present both issues to the Board at  
19 the August Board meeting.

20           We have speakers on this agenda item, after  
21 which we are happy to answer any questions you have.

22           MS. YEE: Great. Thank you, Ms. Buehler.

23           To our speakers, thank you for your patience.  
24 If you'll introduce yourself for the record, you have  
25 two minutes for your comments.

26           Please?

27                           ---o0o---

28                           JULIAN DECYK

1                                ---o0o---

2                    MR. DECYK: Thank you, Ms. Yee. My name's  
3 Julian Decyk. I am with Paul Hastings.

4                    I was co-lead counsel for the taxpayers in  
5 the -- in the Nortel cases. I'm co-author of the two  
6 Paul Hastings letters to which the formal issue paper  
7 here refers.

8                    I'd like to make two points briefly.

9                    First, the formal issue paper states that Paul  
10 Hastings recommended that Regulation 1507 be amended in  
11 a specific manner.

12                   In fact, Paul Hastings in these two letters  
13 made no specific recommendations to amend  
14 Regulation 1507, rather Paul Hastings was responding to  
15 factual errors and misstatements of applicable law  
16 presented in the initial and second discussion papers.

17                   As a result, the purpose of the letters was to  
18 base the discussion for potential amendments to  
19 Regulation 1507 on an accurate statement of the facts  
20 and law, thereby avoiding the potential for developing  
21 an invalid regulation.

22                   As we both know, there have been two invalid  
23 regulations relating to the technology transfer  
24 agreement statutes and we really don't need another.

25                   Moreover, because the statements in the letters  
26 were simply a description of the TTA statutes as  
27 authoritatively interpreted by the courts that  
28 considered them, you don't need a regulation to

1 implement them. They should just be implemented.

2 Second, the Board staff, in their discussion  
3 papers, have in many instances simply failed to  
4 substantially respond in any manner to the factual  
5 corrections and legal analyses presented to them.  
6 Instead in many instances the Board staff's papers  
7 simply repeat unchanged the statement that was refuted.  
8 And the Board staff's papers don't even acknowledge,  
9 much less respond to, the points made to them.

10 This approach leads to nothing constructive.  
11 Moreover, if Board Members read only the Board staff's  
12 position paper, this approach creates a potential -- a  
13 potentially misleading picture of the choices available  
14 to Board Members.

15 Thank you for your consideration.

16 MS. YEE: Thank you.

17 Next, please.

18 ---o0o---

19 MARK NEBERGALL

20 ---o0o---

21 MR. NEBERGALL: Yes, my name's Mark Nebergall.

22 Honorable Members of the Board, I'm the  
23 President of the Software Finance and Executive Council,  
24 which is a trade association that provides public  
25 policy, advocacy in the areas of tax, finance and  
26 accounting for the software industry.

27 I'm also here on behalf of a broadbased  
28 coalition of companies and trade associations that have

1    been participating in the interested parties process on  
2    this issue.

3               And I'm here to tell you today that we support  
4    the direction that the staff has recommended and to just  
5    briefly restate our understanding of the direction they  
6    are recommending that the -- that the issues be split  
7    into two baskets -- one basket having to do with the  
8    software stored on a tangible storage medium and the  
9    other basket for software that's stored on tangible  
10   personal property that is other than a tangible storage  
11   medium and that those issues be considered separately.  
12   We support that.

13              We also ask that you give the Board direction  
14   to consider the proposals that it has received that  
15   suggest that, at least with regard to software stored  
16   on -- or that is sold on tangible personal property  
17   other than a disk -- that a percentage split methodology  
18   approach be considered. We ask that you direct the  
19   staff to look more closely at those proposals and come  
20   up with a regulation that -- that allows companies  
21   and -- to sell products with a clear understanding of  
22   what their sales tax and use tax responsibilities are.

23              With that, I will conclude. And I'm prepared  
24   to answer any questions about the proposals, at least  
25   that SOFTEC and the Silicon Valley Leadership Group has  
26   submitted with regard to these issues.

27              MS. YEE: Thank you, Mr. Nebergall.

28              MR. NEBERGALL: You're welcome.

1 MS. YEE: Ms. Rodriquez.

2 ---o0o---

3 GINA RODRIQUEZ

4 ---o0o---

5 MS. RODRIQUEZ: Gina Rodriquez with the  
6 California Taxpayers Association, thank you very much.

7 First, if -- if there is a need for a  
8 regulation -- and we're not convinced there is, as  
9 Mr. Decyk stated -- we do want to continue working with  
10 staff on some -- some proposed language.

11 Cal-Tax did, in fact, offer some proposed  
12 language to staff not too long ago, sort of  
13 complementing SOFTEC's proposal.

14 There's the software industry and then there's  
15 everybody else that's interested. And, so, we want to  
16 make sure all interests are represented -- all  
17 industries are represented with respect to TTAs.

18 So, we did offer a safe harbor proposal. And  
19 we would love to continue working with staff on that  
20 language.

21 MS. YEE: Great. Thank you very much,  
22 Ms. Rodriquez.

23 Let me just make a couple comments here and I  
24 do support the staff recommendation as well. I think  
25 there has been some movement, albeit we're moving slow  
26 but deliberately on these issues, that it is -- these  
27 are difficult issues.

28 And I think from my perspective, I want to be

1 sure that what the Board does ultimately adopt is on  
2 solid legal foundation.

3 And I also want to be sure that -- and I have  
4 had many conversations with industry representatives  
5 that I think from both of our vantage point we want  
6 whatever is ultimately adopted to be clear with respect  
7 to implementing -- implementation, administration and  
8 certainly compliance in audit requirements as well.

9 This -- there are some pending audits that  
10 encompass some of these issues. And, so, I think  
11 clarity is of the utmost importance.

12 I will also say that I think one of the  
13 breakthroughs was with the submission of the  
14 SOFTEC-Silicon Valley Leadership proposal.

15 And I think Ms. Rodriquez's proposal also, I  
16 would say that at this point everything is still on the  
17 table, that we certainly want clarity.

18 And in order to get ease and compliance and  
19 certainly clear audit guidelines for the Board of  
20 Equalization, we're going to continue to work towards  
21 that goal.

22 So, Members, comments on this?

23 Mr. Horton.

24 MR. HORTON: Thank you, Madam Chair. I think  
25 I, Madam Chair, would like to have just a little more  
26 clarification on the discussion about the need for  
27 regulation or not.

28 MS. YEE: Uh-huh.

1 MR. HORTON: I'd like to hear from the  
2 Department as to their views and then possibly return to  
3 the witnesses that are here from the various groups.

4 MS. YEE: Okay, great question.

5 Mr. Heller.

6 MR. HELLER: Thank you, Ms. Yee.

7 Essentially right now we do already have two  
8 different regulations that we're -- that are already --  
9 already have been adopted, Regulation 1502, which  
10 addresses data processing programming and computer  
11 programs and the second regulation, 1507, that deals  
12 with technology transfer agreements.

13 So, essentially, staff was -- to the extent  
14 that we were going to further define what is a  
15 technology transfer agreement or a change or -- or  
16 include additional contracts in the -- within the  
17 definition, then staff was thinking that it might be the  
18 most appropriate to make those changes in the regulation  
19 that deals with technology transfer agreements.  
20 However, we're still open to looking at that further.

21 And then, in addition, with regard to the  
22 software itself, we do think we have a whole regulation  
23 that just deals with computer programs so that if  
24 there's any treatment of computer programs that's  
25 different than other types of tangible personal -- or I  
26 should say, other types of property, then -- then we  
27 were leaning towards making those amendments in  
28 Regulation 1502 as well.



1 But we're not necessarily arguing that it has  
2 to be done that way and we're open to further discussion  
3 as to the best method to do it.

4 MR. HORTON: Okay, that's helpful.

5 I mean I do believe there needs to be some  
6 clarification or some guidance, if you will, to -- to  
7 the industry as well as to the Audit Department, who  
8 will ultimately be reviewing these transactions.

9 And I think that's important whether that can  
10 be accomplished in the audit manual or some other means  
11 in and of itself is debatable.

12 The regulatory process, by having the  
13 clarification, the Board has historically codified that  
14 in the regulatory process by virtue of -- for the  
15 purpose, if you will, of giving direction to -- to -- to  
16 all who may be considering or may be dealing with the  
17 embedded software issue specifically.

18 And it seems to have a little more weight and a  
19 little more protection for the industry if, in fact, the  
20 ultimate language that is codified sort of represents  
21 the consensus of all of the interested parties to have  
22 it embedded in the regulation, as opposed to providing  
23 the Field Audit Manual adjustment directing the audit  
24 staff, which isn't something the staff -- I mean that  
25 the industry or the taxpayer generally has access to.

26 And, so, they're subject to clarification in  
27 the audit process, as opposed to a method in which we  
28 are communicating.

1           Even though we're not -- I mean I understand  
2   the concerns, but we're not necessarily changing the  
3   law. And the presumption is you are clarifying the  
4   law -- at least from my own personal perspective.

5           I don't want to -- so, Madam Chair, I too would  
6   be supportive of staff recommendation and -- as they  
7   have instructed staff to continue to work with the  
8   industry on the embedded software issue.

9           MS. YEE: Okay. I'll take that as a motion.  
10   Motion by Mr. Horton to adopt the staff recommendation.  
11   Is there a second?

12           MS. STEEL: Second.

13           MS. YEE: Second by Ms. Steel.

14           Without objection, motion carries.

15           Thank you very much.

16           MR. HELLER: Thank you.

17           MS. BUEHLER: In action 2, regarding whether to  
18   amend Regulation 1507, technology transfer agreements to  
19   clarify how the technology transfer under the statutes  
20   apply --

21           MR. HORTON: I think we --

22           MS. MANDEL: I understand the motion to  
23   cover --

24           MS. YEE: To cover both.

25           MS. BUEHLER: All three?

26           MS. YEE: Yes, uh-huh.

27           MS. BUEHLER: 'Cause there are three.

28           MS. MANDEL: There's three?

1 I've got to stop reading just the issue paper.

2 MS. BUEHLER: We're good. If you're good with  
3 all three, I'm good with all three.

4 MR. HORTON: All right, we are.

5 MR. HELLER: Ms. Yee, with your permission, if  
6 I could just make one quick clarification --

7 MS. YEE: Please, Mr. Heller.

8 MR. HELLER: -- it's not impacting the vote at  
9 all.

10 MS. YEE: Yes.

11 MR. HELLER: It was just -- I did want to point  
12 out, though, that staff, at least slightly, misconstrued  
13 Ernst & Young's comments as reflected in the discussion  
14 paper.

15 And to the extent that we are -- staff thought  
16 that the comments might apply to something like a --

17 MS. MANDEL: Coffee maker?

18 MR. HELLER: -- I think we used in there  
19 computer printer, like a normal consumer printer, and  
20 we've been informed that that was not the intent.

21 And we somehow misconstrued it and we're  
22 willing to talk with Ernst & Young further to figure out  
23 what kind of property they were referring to and see  
24 if -- and see how tax applies once we understand the  
25 transaction.

26 MS. YEE: Very well.

27 Thank you for that, Mr. Heller.

28 Okay. Thank you very much.

1 MR. HELLER: Thank you.

2 MS. BUEHLER: Thank you.

3 MS. YEE: That concludes the Business Taxes  
4 Committee for this meeting.

5 Thank you, Ms. Richmond.

6 ---o0o---

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1 REPORTER'S CERTIFICATE.  
2

3 State of California )  
4 ) ss  
5 County of Sacramento )  
6

7 I, KATHLEEN SKIDGEL, Hearing Reporter for the  
8 California State Board of Equalization certify that on  
9 January 15, 2013 I recorded verbatim, in shorthand, to  
10 the best of my ability, the proceedings in the  
11 above-entitled hearing; that I transcribed the shorthand  
12 writing into typewriting; and that the preceding pages 1  
13 through 36 constitute a complete and accurate  
14 transcription of the shorthand writing.  
15

16 Dated: February 20, 2013  
17

18 *Kathleen Skidgel*  
19

20 KATHLEEN SKIDGEL, CSR #9039  
21 Hearing Reporter  
22  
23  
24  
25  
26  
27  
28



**ESTIMATE OF COST OR SAVINGS RESULTING  
FROM PROPOSED REGULATORY ACTION**

**Proposed Amendment of Sales and Use Tax Regulations 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

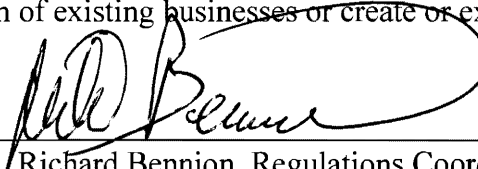
**STATEMENT OF COST OR SAVINGS FOR NOTICE OF PUBLIC HEARING**

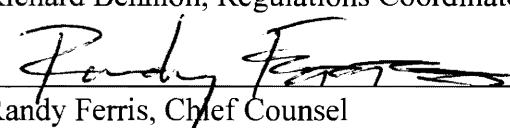
The State Board of Equalization has determined that the proposed action does not impose a mandate on local agencies or school districts. Further, the Board has determined that the action will result in no direct or indirect cost or savings to any State agency, any local agency or school district that is required to be reimbursed under Part 7 (commencing with Section 17500) of Division 4 of Title 2 of the Government Code or other non-discretionary cost or savings imposed on local agencies, or cost or savings in Federal funding to the State of California.

The cost impact on private persons or businesses will be insignificant. This proposal will not have a significant adverse economic impact on businesses.

This proposal will not be detrimental to California businesses in competing with businesses in other states.

This proposal will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses or create or expand business in the State of California.

Statement  
Prepared by  Date 5/6/13  
Richard Bennion, Regulations Coordinator

Approved by  Date 5/6/13  
Randy Ferris, Chief Counsel

**If Costs or Savings are Identified, Signatures of Chief, Fiscal Management Division, and Chief, Board Proceedings Division, are Required**

Approved by \_\_\_\_\_ Date \_\_\_\_\_  
Chief, Financial Management Division

Approved by \_\_\_\_\_ Date \_\_\_\_\_  
Chief, Board Proceedings Division

**NOTE:** SAM Section 6660 requires that estimates resulting in cost or savings be submitted for Department of Finance concurrence before the notice of proposed regulatory action is released.

**ECONOMIC AND FISCAL IMPACT STATEMENT****REGULATIONS AND ORDERS)**

TD. 399 (REV. 12/2008)

**See SAM Section 6601 - 6616 for Instructions and Code Citations**

DEPARTMENT NAME State Board of Equalization	CONTACT PERSON Rick Bennion	TELEPHONE NUMBER 9164452130
DESCRIPTIVE TITLE FROM NOTICE REGISTER OR FORM 400 Service of a Notice of Violation or Warning Notice		NOTICE FILE NUMBER Z

**ECONOMIC IMPACT STATEMENT****A. ESTIMATED PRIVATE SECTOR COST IMPACTS** (Include calculations and assumptions in the rulemaking record.)

1. Check the appropriate box(es) below to indicate whether this regulation:

- |   |  |
|---|--|
| <input type="checkbox"/> a. Impacts businesses and/or employees | <input type="checkbox"/> e. Imposes reporting requirements   |
| <input type="checkbox"/> b. Impacts small businesses            | <input type="checkbox"/> f. Imposes prescriptive instead of performance  |
| <input type="checkbox"/> c. Impacts jobs or occupations         | <input type="checkbox"/> g. Impacts individuals  |
| <input type="checkbox"/> d. Impacts California competitiveness  | <input checked="" type="checkbox"/> h. None of the above (Explain below. Complete the Fiscal Impact Statement as appropriate.) |

h. (cont.) Please see the attached .

(If any box in Items 1 a through g is checked, complete this Economic Impact Statement.)

2. Enter the total number of businesses impacted: \_\_\_\_\_ Describe the types of businesses (Include nonprofits.): \_\_\_\_\_

Enter the number or percentage of total businesses impacted that are small businesses: \_\_\_\_\_

. Enter the number of businesses that will be created: \_\_\_\_\_ eliminated: \_\_\_\_\_

Explain: \_\_\_\_\_

4. Indicate the geographic extent of impacts: ☐ Statewide ☐ Local or regional (List areas.): \_\_\_\_\_

5. Enter the number of jobs created: \_\_\_\_\_ or eliminated: \_\_\_\_\_ Describe the types of jobs or occupations impacted: \_\_\_\_\_

6. Will the regulation affect the ability of California businesses to compete with other states by making it more costly to produce goods or services here?

☐ Yes ☐ No If yes, explain briefly: \_\_\_\_\_**B. ESTIMATED COSTS** (Include calculations and assumptions in the rulemaking record.)

1. What are the total statewide dollar costs that businesses and individuals may incur to comply with this regulation over its lifetime? \$ \_\_\_\_\_

a. Initial costs for a small business: \$ \_\_\_\_\_ Annual ongoing costs: \$ \_\_\_\_\_ Years: \_\_\_\_\_

b. Initial costs for a typical business: \$ \_\_\_\_\_ Annual ongoing costs: \$ \_\_\_\_\_ Years: \_\_\_\_\_

c. Initial costs for an individual: \$ \_\_\_\_\_ Annual ongoing costs: \$ \_\_\_\_\_ Years: \_\_\_\_\_

d. Describe other economic costs that may occur: \_\_\_\_\_

**ECONOMIC AND FISCAL IMPACT STATEMENT cont. (STD. 399, Rev. 12/2008)**

2. If multiple industries are impacted, enter the share of total costs for each industry: \_\_\_\_\_  
\_\_\_\_\_

3. If the regulation imposes reporting requirements, enter the annual costs a typical business may incur to comply with these requirements. (Include the dollar costs to do programming, record keeping, reporting, and other paperwork, whether or not the paperwork must be submitted.): \$ \_\_\_\_\_

4. Will this regulation directly impact housing costs? ☐ Yes ☐ No If yes, enter the annual dollar cost per housing unit: \_\_\_\_\_ and the number of units: \_\_\_\_\_

5. Are there comparable Federal regulations? ☐ Yes ☐ No Explain the need for State regulation given the existence or absence of Federal regulations: \_\_\_\_\_

Enter any additional costs to businesses and/or individuals that may be due to State - Federal differences: \$ \_\_\_\_\_

---

**C. ESTIMATED BENEFITS** (Estimation of the dollar value of benefits is not specifically required by rulemaking law, but encouraged.)

---

1. Briefly summarize the benefits that may result from this regulation and who will benefit: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

2. Are the benefits the result of: ☐ specific statutory requirements, or ☐ goals developed by the agency based on broad statutory authority?

Explain: \_\_\_\_\_

3. What are the total statewide benefits from this regulation over its lifetime? \$ \_\_\_\_\_

---

**D. ALTERNATIVES TO THE REGULATION** (Include calculations and assumptions in the rulemaking record. Estimation of the dollar value of benefits is not specifically required by rulemaking law, but encouraged.)

---

1. List alternatives considered and describe them below. If no alternatives were considered, explain why not: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

2. Summarize the total statewide costs and benefits from this regulation and each alternative considered:

Regulation:	Benefit: \$ _____	Cost: \$ _____
Alternative 1:	Benefit: \$ _____	Cost: \$ _____
Alternative 2:	Benefit: \$ _____	Cost: \$ _____

3. Briefly discuss any quantification issues that are relevant to a comparison of estimated costs and benefits for this regulation or alternatives: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

4. Rulemaking law requires agencies to consider performance standards as an alternative, if a regulation mandates the use of specific technologies or equipment, or prescribes specific actions or procedures. Were performance standards considered to lower compliance costs? ☐ Yes ☐ No

Explain: \_\_\_\_\_

---

**E. MAJOR REGULATIONS** (Include calculations and assumptions in the rulemaking record.) Cal/EPA boards, offices, and departments are subject to the following additional requirements per Health and Safety Code section 57005.

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## ECONOMIC AND FISCAL IMPACT STATEMENT cont. (STD. 399, Rev. 12/2008)

1. Will the estimated costs of this regulation to California business enterprises exceed \$10 million ? ☐ Yes ☐ No (If No, skip the rest of this section.)

2. Briefly describe each equally as an effective alternative, or combination of alternatives, for which a cost-effectiveness analysis was performed:

Alternative 1: \_\_\_\_\_

Alternative 2: \_\_\_\_\_

3. For the regulation, and each alternative just described, enter the estimated total cost and overall cost-effectiveness ratio:

Regulation: \$ \_\_\_\_\_ Cost-effectiveness ratio: \$ \_\_\_\_\_

Alternative 1: \$ \_\_\_\_\_ Cost-effectiveness ratio: \$ \_\_\_\_\_

Alternative 2: \$ \_\_\_\_\_ Cost-effectiveness ratio: \$ \_\_\_\_\_

### FISCAL IMPACT STATEMENT

A. FISCAL EFFECT ON LOCAL GOVERNMENT (Indicate appropriate boxes 1 through 6 and attach calculations and assumptions of fiscal impact for the current year and two subsequent Fiscal Years.)

☐ 1. Additional expenditures of approximately \$ \_\_\_\_\_ in the current State Fiscal Year which are reimbursable by the State pursuant to Section 6 of Article XIII B of the California Constitution and Sections 17500 et seq. of the Government Code. Funding for this reimbursement:

☐ a. is provided in \_\_\_\_\_, Budget Act of \_\_\_\_\_ or Chapter \_\_\_\_\_, Statutes of \_\_\_\_\_

☐ b. will be requested in the \_\_\_\_\_ Governor's Budget for appropriation in Budget Act of \_\_\_\_\_  
(FISCAL YEAR)

☐ 2. Additional expenditures of approximately \$ \_\_\_\_\_ in the current State Fiscal Year which are not reimbursable by the State pursuant to Section 6 of Article XIII B of the California Constitution and Sections 17500 et seq. of the Government Code because this regulation:

☐ a. implements the Federal mandate contained in \_\_\_\_\_

☐ b. implements the court mandate set forth by the \_\_\_\_\_  
court in the case of \_\_\_\_\_ vs. \_\_\_\_\_

☐ c. implements a mandate of the people of this State expressed in their approval of Proposition No. \_\_\_\_\_ at the \_\_\_\_\_  
election; (DATE)

☐ d. is issued only in response to a specific request from the \_\_\_\_\_  
\_\_\_\_\_, which is/are the only local entity(s) affected;

☐ e. will be fully financed from the \_\_\_\_\_ authorized by Section \_\_\_\_\_  
(FEES, REVENUE, ETC.)  
\_\_\_\_\_ of the \_\_\_\_\_ Code;

☐ f. provides for savings to each affected unit of local government which will, at a minimum, offset any additional costs to each such unit;

☐ g. creates, eliminates, or changes the penalty for a new crime or infraction contained in \_\_\_\_\_

☐ 3. Savings of approximately \$ \_\_\_\_\_ annually.

☐ 4. No additional costs or savings because this regulation makes only technical, non-substantive or clarifying changes to current law regulations.

**ECONOMIC AND FISCAL IMPACT STATEMENT cont. (STD. 399, Rev. 2-98)**

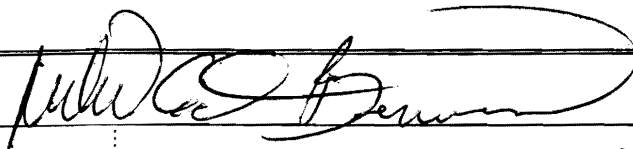


- ☒ 5. No fiscal impact exists because this regulation does not affect any local entity or program.
- ☐ 6. Other.

**B. FISCAL EFFECT ON STATE GOVERNMENT** *(Indicate appropriate boxes 1 through 4 and attach calculations and assumptions of fiscal impact for the current year and two subsequent Fiscal Years.)*

- ☐ 1. Additional expenditures of approximately \$ \_\_\_\_\_ in the current State Fiscal Year. It is anticipated that State agencies will:
- ☐ a. be able to absorb these additional costs within their existing budgets and resources.
- ☐ b. request an increase in the currently authorized budget level for the \_\_\_\_\_ fiscal year.
- ☐ 2. Savings of approximately \$ \_\_\_\_\_ in the current State Fiscal Year.
- ☒ 3. No fiscal impact exists because this regulation does not affect any State agency or program.
- ☐ 4. Other.

**C. FISCAL EFFECT ON FEDERAL FUNDING OF STATE PROGRAMS** *(Indicate appropriate boxes 1 through 4 and attach calculations and assumptions of fiscal impact for the current year and two subsequent Fiscal Years.)*

- ☐ 1. Additional expenditures of approximately \$ \_\_\_\_\_ in the current State Fiscal Year.
- ☐ 2. Savings of approximately \$ \_\_\_\_\_ in the current State Fiscal Year.
- ☒ 3. No fiscal impact exists because this regulation does not affect any federally funded State agency or program.
- ☐ 4. Other.

SIGNATURE 		TITLE Regulations Coordinator
AGENCY SECRETARY <sup>1</sup>	APPROVAL/CONCURRENCE  PROGRAM BUDGET MANAGER	DATE 4-9-13
DEPARTMENT OF FINANCE <sup>2</sup>		DATE
APPROVAL/CONCURRENCE 	Exempt under SAM section 6660	

- The signature attests that the agency has completed the STD. 399 according to the instructions in SAM sections 6600-6680, and understands the impacts of the proposed rulemaking. State boards, offices, or departments not under an Agency Secretary must have the form signed by the highest ranking official in the organization.
- Finance approval and signature is required when SAM sections 6600-6670 require completion of the Fiscal Impact Statement in the STD. 399.

**Attachment to Economic and Fiscal Impact**  
**Statement (STD. 399 (Rev. 12/2008)) for the Proposed Amendments to**  
**California Code of Regulations, Title 18, Sections 4601, *Service of a Notice of***  
***Violation or Warning Notice*, 4603, *Penalties for Licensed and Unlicensed***  
***Retailers*, 4604, *Penalties for Licensed and Unlicensed Wholesalers and***  
***Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers***  
***and Importers***

The Cigarette and Tobacco Products Licensing Act (Act) (division 8.6 (commencing with § 22970) of the Business and Professions Code (BPC)) imposes licensing requirements on all retailers, wholesalers, distributors, manufacturers and importers of cigarettes and tobacco products. The Act is administered by the State Board of Equalization (Board) pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements.

As relevant here, the Board adopted California Code of Regulations, title 18, sections (Regulations) 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, and 4601, *Service of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to and serve such notice on a person that has been issued a citation for a violation of the Act. The Board also adopted Regulations 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*, to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant.

The proposed amendments to Regulation 4601 simply require all notices issued under the Act to be served in the manner provided by BPC section 22971.5 for the service of notices under the Act. As such, the amendments merely make the regulation consistent with the applicable statute regarding the service of such notices.

Furthermore, Regulations 4603 through 4605 already give the Board discretion to reduce a suspension period to 0 days, 10 days, or 20 days when mitigating factors are present. The proposed amendments to Regulations 4603 through 4605 will also permit the Board to reduce a suspension period to 5 days when mitigating factors are present. The Board intends to use the 5-day suspension period in those situations where the Board would currently impose a 10-day suspension, but the Board determines that a 10-day suspension would be too harsh, and the Board does not intend to use the 5-day suspension period where the Board would currently reduce a suspension period to 0 days. Therefore, the Board anticipates that some persons will benefit from the proposed amendments by having their suspensions reduced to 5 days instead of 10 days.

Therefore, based upon the foregoing information and all of the information in the rulemaking file, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605:

- Will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states;
- Will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California;
- Will not have a significant effect on housing costs;
- Will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California; and
- Will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

In addition, the Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed regulatory action.

**NOTICE PUBLICATION/REGULATIONS SUBMISSION**(See instructions on  
reverse)

For use by Secretary of State only

STD. 400 (REV. 01-2013)

<b>OAL FILE NUMBERS</b>	<b>NOTICE FILE NUMBER</b> Z-2013-0409-01	<b>REGULATORY ACTION NUMBER</b>	<b>EMERGENCY NUMBER</b>
For use by Office of Administrative Law (OAL) only			
<b>RECEIVED FOR FILING PUBLICATION DATE</b>  APR 09 '13      APR 19 '13  <b>Office of Administrative Law</b> NOTICE		REGULATIONS	

AGENCY WITH RULEMAKING AUTHORITY

AGENCY FILE NUMBER (If any)

**A. PUBLICATION OF NOTICE (Complete for publication in Notice Register)**

<b>1. SUBJECT OF NOTICE</b> Service of a Notice of Violation or Warning Notice		<b>TITLE(S)</b> 18	<b>FIRST SECTION AFFECTED</b> 4601	<b>2. REQUESTED PUBLICATION DATE</b> April 19, 2013
<b>3. NOTICE TYPE</b> <input checked="" type="checkbox"/> Notice re Proposed Regulatory Action <input type="checkbox"/> Other		<b>4. AGENCY CONTACT PERSON</b> Richard E. Bennion	<b>TELEPHONE NUMBER</b> (916) 445-2130	<b>FAX NUMBER (Optional)</b> (916) 324-3984
<b>OAL USE ONLY</b>	<b>ACTION ON PROPOSED NOTICE</b> <input type="checkbox"/> Approved as Submitted <input type="checkbox"/> Approved as Modified <input type="checkbox"/> Disapproved/Withdrawn		<b>NOTICE REGISTER NUMBER</b>	<b>PUBLICATION DATE</b>

**B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)**

<b>1a. SUBJECT OF REGULATION(S)</b>		<b>1b. ALL PREVIOUS RELATED OAL REGULATORY ACTION NUMBER(S)</b>	
<b>SPECIFY CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)</b>			
<b>SECTION(S) AFFECTED</b> (List all section number(s) individually. Attach additional sheet if needed.)	ADOPT		
	AMEND		
	REPEAL		
<b>3. TYPE OF FILING</b>			
<input type="checkbox"/> Regular Rulemaking (Gov. Code §11346) <input type="checkbox"/> Resubmittal of disapproved or withdrawn nonemergency filing (Gov. Code §§11349.3, 11349.4) <input type="checkbox"/> Emergency (Gov. Code, §11346.1(b))			
<input type="checkbox"/> Certificate of Compliance: The agency officer named below certifies that this agency complied with the provisions of Gov. Code §§11346.2-11347.3 either before the emergency regulation was adopted or within the time period required by statute. <input type="checkbox"/> Resubmittal of disapproved or withdrawn emergency filing (Gov. Code, §11346.1)			
<input type="checkbox"/> Emergency Readopt (Gov. Code, §11346.1(h)) <input type="checkbox"/> File & Print <input type="checkbox"/> Other (Specify) _____			
<input type="checkbox"/> Changes Without Regulatory Effect (Cal. Code Regs., title 1, §100) <input type="checkbox"/> Print Only			
<b>4. ALL BEGINNING AND ENDING DATES OF AVAILABILITY OF MODIFIED REGULATIONS AND/OR MATERIAL ADDED TO THE RULEMAKING FILE (Cal. Code Regs. title 1, §44 and Gov. Code §11347.1)</b>			
<b>5. EFFECTIVE DATE OF CHANGES (Gov. Code, §§ 11343.4, 11346.1(d); Cal. Code Regs., title 1, §100)</b>			
<input type="checkbox"/> Effective January 1, April 1, July 1, or October 1 (Gov. Code §11343.4(a)) <input type="checkbox"/> Effective on filing with Secretary of State <input type="checkbox"/> \$100 Changes Without Regulatory Effect <input type="checkbox"/> Effective other (Specify) _____			
<b>6. CHECK IF THESE REGULATIONS REQUIRE NOTICE TO, OR REVIEW, CONSULTATION, APPROVAL OR CONCURRENCE BY, ANOTHER AGENCY OR ENTITY</b>			
<input type="checkbox"/> Department of Finance (Form STD. 399) (SAM §6660) <input type="checkbox"/> Fair Political Practices Commission <input type="checkbox"/> State Fire Marshal <input type="checkbox"/> Other (Specify) _____			
<b>7. CONTACT PERSON</b>		<b>TELEPHONE NUMBER</b>	<b>FAX NUMBER (Optional)</b>
			<b>E-MAIL ADDRESS (Optional)</b>

8. I certify that the attached copy of the regulation(s) is a true and correct copy of the regulation(s) identified on this form, that the information specified on this form is true and correct, and that I am the head of the agency taking this action, or a designee of the head of the agency, and am authorized to make this certification.

For use by Office of Administrative Law (OAL) only

<b>SIGNATURE OF AGENCY HEAD OR DESIGNEE</b>	<b>DATE</b>
<b>TYPED NAME AND TITLE OF SIGNATORY</b>	

## **Notice of Proposed Regulatory Action**

### **The State Board of Equalization Proposes to Adopt Amendments to California Code of Regulations, Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

#### **NOTICE IS HEREBY GIVEN**

The State Board of Equalization (Board), pursuant to the authority vested in it by Business and Professions Code (BPC) section 22971.2, proposes to adopt amendments to California Code of Regulations, title 18, sections (Regulations) 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*. The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) (div. 8.6 (commencing with § 22970) of the BPC) to be served personally or by mail in the manner prescribed for service of a notice under BPC section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

#### **PUBLIC HEARING**

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 11, 2013. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on June 11, 2013. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605.

#### **AUTHORITY**

BPC section 22971.2.

## REFERENCE

- Regulation 4601: BPC section 22971.5
- Regulation 4603: BPC sections 22973, 22974, 22974.3, 22974.4, 22974.7, 22980, 22980.1, 22980.2, and 22980.3
- Regulation 4604: BPC sections 22974.7, 22977, 22978.1, 22978.2, 22978.5, 22978.7, 22979.7, 22980, 22980.1, 22980.2, and 22980.3
- Regulation 4605: BPC sections 22974.7, 22979, 22979.4, 22979.5, 22979.6, 22979.7, 22980.1, 22980.2, and 22980.3

## INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

### Current Law

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Act to the BPC. As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the Board pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted Regulation 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to a person that has been issued a citation for a violation of the Act, and the Board adopted Regulation 4601 to prescribe the manner in which a Notice of Violation or Warning Notice shall be served. The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, 4604, and 4605 to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

Effect, Objectives, and Benefits of the Proposed Amendments to Regulations 4601, 4603, 4604, and 4605

*Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, the intent and objectives of the proposed amendments to Regulation 4601 are to make the regulation prescribe the manner of serving all of the notices the Board is required to serve under the Act, require that all of the notices be served in the manner prescribed for service of a notice under BPC section 22971.5, and generally ensure that the regulation is consistent with BPC section 22971.5. The Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

The text of the proposed amendments to Regulation 4601 is slightly different than the text that the Board approved on June 26, 2012. The original text provided that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law.” However, section 22971.5 was added to the BPC after the Board’s adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised the approved text of the amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board’s proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board’s proposed amendments provide that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5.”

*Amendments to Regulations 4603 through 4605*



Regulations 4603 through 4605 provide that a suspension period may be reduced to “0 days, 10 days, or 20 days” when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10 days would be appropriate. The intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to add a 5-day suspension period to the regulations to specifically give the Board additional flexibility to reduce suspensions based upon staff’s belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, the intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to clarify the regulations’ cross-references to statutes that require the revocation of retailers’, wholesalers’, distributors’, manufacturers’, and importers’ licenses for specified violations of the Act; and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

The proposed amendments also update the reference notes to Regulations 4601, 4603, 4604, and 4605 to better reflect the contents of each reference note’s regulation.

#### *Business Taxes Committee Process*

The Board approved the amendments to Regulation 4601, 4603, 4604, and 4605 (described above) during the Board’s June 26, 2012, Business Taxes Committee meeting, but, at the conclusion of the meeting, the Board voted to postpone proposing the amendments to Regulations 4601, 4603, 4604, and 4605 while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other provisions of the Act. During the Board’s January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 at this time, and the Board did not decide to propose to adopt a new regulation at that time.

The Board has performed an evaluation of whether the proposed amendments to Regulations 4601, 4603, 4604, and 4605 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 4601 is the only state regulation prescribing the manner for serving a notice issued under the Act and Regulations 4603 through 4605 are the only state regulations prescribing the Board’s discretion to reduce a suspension imposed under the Act. In addition, there are no comparable federal regulations or statutes to Regulations 4601, 4603, 4604, and 4605.

## NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

## NO COST OR SAVINGS TO STATE AGENCIES, LOCAL AGENCIES, AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

## NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The Board has made an initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 may affect small business.

## NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

The Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

## RESULTS OF THE ECONOMIC IMPACT ANALYSIS REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

## NO SIGNIFICANT EFFECT ON HOUSING COSTS

Adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant effect on housing costs.

## DETERMINATION REGARDING ALTERNATIVES

The Board must determine that no reasonable alternative considered by it or that has been otherwise identified and brought to its attention would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

## CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at [Bradley.Heller@boe.ca.gov](mailto:Bradley.Heller@boe.ca.gov), or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at [Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

## WRITTEN COMMENT PERIOD

The written comment period ends at 10:00 a.m. on June 11, 2013, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulations 4601, 4603, 4604, and 4605 during the June 11, 2013, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605. The Board will only consider written comments received by that time.

## AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared underscored and strikeout versions of the text of Regulations 4601, 4603, 4604, and 4605 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which

includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

#### SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

#### AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulations 4601, 4603, 4604, and 4605, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

**Text of Proposed Amendments to  
California Code of Regulations, Title 18, Sections  
4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*,  
4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and  
4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

**4601. Service of a Notice of Violation or Warning Notice.**

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5. The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub-post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22971.5~~22974.7~~, ~~22978.7~~ and ~~22979.7~~, Business and Professions Code.

**4603. Penalties for Licensed or Unlicensed Retailers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

(1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).

(2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).

(3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, ~~22978.6~~, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22973(a)(5), 22974, 22974.3, 22974.4, 22974.7, 22980.1(c), (d), (e) and (g), 22980(b), 22980.2(a) and 22980.3(a)(2) and (d), Business and Professions Code.

#### **4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).
- (2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).
- (3) Business and Professions Code section 22978.5. subdivision (b) (distributor's or wholesaler's failure to retain sales records).
- (4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

- (1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).
- (2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4~~22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, 22977(a)(5), 22978.1, 22978.2, ~~22978.7~~, 22978.5(b), 22978.7, 22979.7, 22980(b), 22980.1(b), (c), (d), (e), (f) and (g), ~~and 22980.2(a) and 22980.3(a)(2) and (d),~~ Business and Professions Code.

#### **4605. Penalties for Licensed or Unlicensed Manufacturers and Importers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:



(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).
- (2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).
- (3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).
- (4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).
- (6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

(b) A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)) shall result in a 20-day suspension.

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

(d) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, ~~22978.7, 22979.4, 22979(b)(1), 22979.4, 22979.5(b), 22979.6(c), 22979.7, 22980.1(a), (e) and (f), 22980.2(a), and 22980.3(a)(2) and (d)~~ ~~22979.6(e),~~ Business and Professions Code.

## Bennion, Richard

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**From:** BOE-Board Meeting Material  
**Sent:** Friday, April 19, 2013 11:54 AM  
**To:** Alonzo, Mary Ann (Legal); Angeja, Jeff (Legal); Angeles, Joel; Armenta, Christopher; Bartolo, Lynn; Bennion, Richard; Benson, Bill; Bisauta, Christine (Legal); Blake, Sue; BOE-Board Meeting Material; Bridges, Cynthia; Chung, Sophia (Legal); Davis, Toya P.; Delgado, Maria; Duran, David; Elliott, Claudia; Epolite, Anthony (Legal); Ferris, Randy (Legal); Ford, Ladeena L; Garcia, Laura; Gau, David; Gilman, Todd; Giorgi, Alan; Giorgi, Dolores; Goehring, Teresa; Hale, Mike; Hamilton, Tabitha; Hanohano, Rebecca; Harvill, Mai; He, Mengjun; Heller, Bradley (Legal); Hellmuth, Leila; Herrera, Cristina; Holmes, Dana; Hughes, Shellie L; Jacobson, Andrew; Kinkle, Sherrie L; Kinst, Lynne; Kuhl, James; Lambert, Robert (Legal); Levine, David H. (Legal); LoFaso, Alan; Madrigal, Claudia; Maeng, Elizabeth; Mandel, Marcy Jo; Matsumoto, Sid; McGuire, Jeff; Miller, Brad; Mandel, Marcy Jo @ SCO; Moon, Richard (Legal); Morquecho, Raymond; Nienow, Trecia (Legal); Pielsticker, Michele; Ralston, Natasha; Richmond, Joann; Riley, Denise (Legal); Salgado-Ponce, Sylvia; Schultz, Glenna; Shah, Neil; Silva, Monica; Singh, Sam; Smith, Kevin (Legal); Smith, Rose; Stowers, Yvette; Suero-Gabler, Cynthia; Torres, Rodrigo; Torres, Rodrigo; Tran, Mai (Legal); Treichelt, Tim; Tucker, Robert (Legal); Vasquez, Rosalyn; Vasquez, Rosalyn; Vassar, Alex; Vigil, Michael; Wallentine, Sean; Whitaker, Lynn; White, Sharon; Williams, Lee; Zivkovich, Robert  
**Subject:** State Board of Equalization - Announcement of Regulatory Change 4601, 4603, 4604, and 4605

The State Board of Equalization proposes to amend Regulations 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importer*. A public hearing regarding the proposed amendments will be held in Room 121, 450 N Street, Sacramento, California, at 10:00 a.m., or as soon thereafter as the matter may be heard on June 11, 2013.

The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) to be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code (BPC) section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments also clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

To view the notice of hearing, initial statement of reasons, proposed text, and history click on the following link:  
[http://www.boe.ca.gov/regs/reg\\_4601\\_4603\\_4604\\_4605\\_2013.htm](http://www.boe.ca.gov/regs/reg_4601_4603_4604_4605_2013.htm)

Questions regarding the substance of the proposed amendments should be directed to Mr. Bradley Heller, Tax Counsel IV, at 450 N Street, MIC:82, Sacramento, CA 94279-0082, email [Bradley.Heller@boe.ca.gov](mailto:Bradley.Heller@boe.ca.gov), telephone (916) 323-3091, or FAX (916) 323-3387.

Written comments for the Board's consideration, notices of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed regulatory action should be directed to Mr. Rick Bennion, Regulations Coordinator, telephone (916) 445-2130, fax (916) 324-3984, e-mail [Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov) or by mail to: State Board of Equalization, Attn: Rick Bennion, MIC: 80, P.O. Box 942879-0080, Sacramento, CA 94279-0080.

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Please do not reply to this message.

Board Proceedings Division, MIC:80  
Rick Bennion  
Regulations Coordinator  
Phone (916) 445-2130  
Fax (916) 324-3984  
[Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov)

## Bennion, Richard

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**From:** State Board of Equalization - Announcement of Regulatory Change  
[Legal.Regulations@BOE.CA.GOV]  
**Sent:** Friday, April 19, 2013 1:26 PM  
**To:** BOE\_REGULATIONS@LISTSERV.STATE.CA.GOV  
**Subject:** State Board of Equalization - Announcement of Regulatory Changes to Regulations 4601, 4603, 4604, and 4605

The State Board of Equalization proposes to amend Regulations 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importer*. A public hearing regarding the proposed amendments will be held in Room 121, 450 N Street, Sacramento, California, at 10:00 a.m., or as soon thereafter as the matter may be heard on June 11, 2013.

The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) to be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code (BPC) section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments also clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

To view the notice of hearing, initial statement of reasons, proposed text, and history click on the following link:  
[http://www.boe.ca.gov/regs/reg\\_4601\\_4603\\_4604\\_4605\\_2013.htm](http://www.boe.ca.gov/regs/reg_4601_4603_4604_4605_2013.htm)

Questions regarding the substance of the proposed amendments should be directed to Mr. Bradley Heller, Tax Counsel IV, at 450 N Street, MIC:82, Sacramento, CA 94279-0082, email [Bradley.Heller@boe.ca.gov](mailto:Bradley.Heller@boe.ca.gov), telephone (916) 323-3091, or FAX (916) 323-3387.

Written comments for the Board's consideration, notices of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed regulatory action should be directed to Mr. Rick Bennion, Regulations Coordinator, telephone (916) 445-2130, fax (916) 324-3984, e-mail [Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov) or by mail to: State Board of Equalization, Attn: Rick Bennion, MIC: 80, P.O. Box 942879-0080, Sacramento, CA 94279-0080.

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Please do not reply to this message.

Board Proceedings Division, MIC:80  
Rick Bennion  
Regulations Coordinator  
Phone (916) 445-2130  
Fax (916) 324-3984  
[Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov)

Fair Political Practices Commission, 428 J Street, Suite 620, Sacramento, California 95814, telephone (916) 322-5660.

# AVAILABILITY OF PROPOSED CONFLICT-OF-INTEREST CODES

Copies of the proposed conflict-of-interest codes may be obtained from the Commission offices or the respective agency. Requests for copies from the Commission should be made to Adrienne Tackley, Fair Political Practices Commission, 428 J Street, Suite 620, Sacramento, California 95814, telephone (916) 322-5660.

## TITLE 18. BOARD OF EQUALIZATION

**Amendments to California Code of Regulations, Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

### NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Business and Professions Code (BPC) section 22971.2, proposes to adopt amendments to California Code of Regulations, title 18, sections (Regulations) 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*. The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) (div. 8.6 (commencing with § 22970) of the BPC) to be served personally or by mail in the manner prescribed for service of a notice under BPC section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

### PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 11, 2013. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on June 11, 2013. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605.

### AUTHORITY

BPC section 22971.2.

### REFERENCE

Regulation 4601: BPC section 22971.5  
Regulation 4603: BPC sections 22973, 22974, 22974.3, 22974.4, 22974.7, 22980, 22980.1, 22980.2, and 22980.3  
Regulation 4604: BPC sections 22974.7, 22977, 22978.1, 22978.2, 22978.5, 22978.7, 22979.7, 22980, 22980.1, 22980.2, and 22980.3  
Regulation 4605: BPC sections 22974.7, 22979, 22979.4, 22979.5, 22979.6, 22979.7, 22980.1, 22980.2, and 22980.3

### INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

#### Current Law

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Act to the BPC. As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the Board pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted Regulation 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to a person that has been issued a citation for a violation of the Act, and the Board adopted Regulation 4601 to prescribe the manner in which a Notice of Violation or Warning Notice shall be served. The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, 4604, and 4605 to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

#### Effect, Objectives, and Benefits of the Proposed Amendments to Regulations 4601, 4603, 4604, and 4605

##### *Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal — Special Taxes and Fees Division*, 4701, *Appeal — Appeals Division*, and 4702, *Appeal — Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, the intent and objectives of the proposed amendments to Regulation 4601 are to make the regulation prescribe the manner of serving all of the notices the Board is required to serve under the

Act, require that all of the notices be served in the manner prescribed for service of a notice under BPC section 22971.5, and generally ensure that the regulation is consistent with BPC section 22971.5. The Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

The text of the proposed amendments to Regulation 4601 is slightly different than the text that the Board approved on June 26, 2012. The original text provided that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law." However, section 22971.5 was added to the BPC after the Board's adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised the approved text of the amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board's proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board's proposed amendments provide that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5."

##### *Amendments to Regulations 4603 through 4605*

Regulations 4603 through 4605 provide that a suspension period may be reduced to "0 days, 10 days, or 20 days" when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10 days would be appropriate. The intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to add a 5-day suspension period to the regulations to specifically give the Board additional flexibility to reduce suspensions based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, the intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to

clarify the regulations' cross-references to statutes that require the revocation of retailers', wholesalers', distributors', manufacturers', and importers' licenses for specified violations of the Act; and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

The proposed amendments also update the reference notes to Regulations 4601, 4603, 4604, and 4605 to better reflect the contents of each reference note's regulation.

*Business Taxes Committee Process*

The Board approved the amendments to Regulation 4601, 4603, 4604, and 4605 (described above) during the Board's June 26, 2012, Business Taxes Committee meeting, but, at the conclusion of the meeting, the Board voted to postpone proposing the amendments to Regulations 4601, 4603, 4604, and 4605 while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other provisions of the Act. During the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rule-making process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 at this time, and the Board did not decide to propose to adopt a new regulation at that time.

The Board has performed an evaluation of whether the proposed amendments to Regulations 4601, 4603, 4604, and 4605 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 4601 is the only state regulation prescribing the manner for serving a notice issued under the Act and Regulations 4603 through 4605 are the only state regulations prescribing the Board's discretion to reduce a suspension imposed under the Act. In addition, there are no comparable federal regulations or statutes to Regulations 4601, 4603, 4604, and 4605.

**NO MANDATE ON LOCAL AGENCIES AND  
SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

**NO COST OR SAVINGS TO STATE AGENCIES,  
LOCAL AGENCIES, AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

**NO SIGNIFICANT STATEWIDE ADVERSE  
ECONOMIC IMPACT DIRECTLY  
AFFECTING BUSINESS**

The Board has made an initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 may affect small business.

**NO COST IMPACTS TO PRIVATE PERSONS  
OR BUSINESSES**

The Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

**RESULTS OF THE ECONOMIC IMPACT  
ANALYSIS REQUIRED BY GOVERNMENT  
CODE SECTION 11346.3, SUBDIVISION (b)**

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

### **NO SIGNIFICANT EFFECT ON HOUSING COSTS**

Adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant effect on housing costs.

### **DETERMINATION REGARDING ALTERNATIVES**

The Board must determine that no reasonable alternative considered by it or that has been otherwise identified and brought to its attention would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

### **CONTACT PERSONS**

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at [Bradley.Heller@boe.ca.gov](mailto:Bradley.Heller@boe.ca.gov), or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at [Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

### **WRITTEN COMMENT PERIOD**

The written comment period ends at 10:00 a.m. on June 11, 2013, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulations 4601, 4603, 4604, and 4605 during the June 11, 2013, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to

adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605. The Board will only consider written comments received by that time.

### **AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION**

The Board has prepared underscored and strikethrough versions of the text of Regulations 4601, 4603, 4604, and 4605 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

### **SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8**

The Board may adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

### **AVAILABILITY OF FINAL STATEMENT OF REASONS**

If the Board adopts the proposed amendments to Regulations 4601, 4603, 4604, and 4605, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).



STATE OF CALIFORNIA

**STATE BOARD OF EQUALIZATION**

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Second District, Lancaster

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Third District, Rolling Hills Estates

JEROME E. HORTON  
Fourth District, Los Angeles

JOHN CHIANG  
State Controller

CYNTHIA BRIDGES  
Executive Director

**April 19, 2013**

**To Interested Parties:**

**Notice of Proposed Regulatory Action  
by the  
State Board of Equalization**

**Proposes to Amendments to California Code of Regulations, Title 18,  
Sections 4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for  
Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties  
for Licensed or Unlicensed Manufacturers and Importers***

**NOTICE IS HEREBY GIVEN**

The State Board of Equalization (Board), pursuant to the authority vested in it by Business and Professions Code (BPC) section 22971.2, proposes to adopt amendments to California Code of Regulations, title 18, sections (Regulations) 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*. The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) (div. 8.6 (commencing with § 22970) of the BPC) to be served personally or by mail in the manner prescribed for service of a notice under BPC section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.



## **PUBLIC HEARING**

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 11, 2013. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on June 11, 2013. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605.

## **AUTHORITY**

BPC section 22971.2.

## **REFERENCE**

Regulation 4601:	BPC section 22971.5
Regulation 4603:	BPC sections 22973, 22974, 22974.3, 22974.4, 22974.7, 22980, 22980.1, 22980.2, and 22980.3
Regulation 4604:	BPC sections 22974.7, 22977, 22978.1, 22978.2, 22978.5, 22978.7, 22979.7, 22980, 22980.1, 22980.2, and 22980.3
Regulation 4605:	BPC sections 22974.7, 22979, 22979.4, 22979.5, 22979.6, 22979.7, 22980.1, 22980.2, and 22980.3

## **INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW**

### Current Law

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Act to the BPC. As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the

Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the Board pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted Regulation 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to a person that has been issued a citation for a violation of the Act, and the Board adopted Regulation 4601 to prescribe the manner in which a Notice of Violation or Warning Notice shall be served. The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, 4604, and 4605 to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

Effect, Objectives, and Benefits of the Proposed Amendments to Regulations 4601, 4603, 4604, and 4605

#### *Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, the intent and objectives of the proposed amendments to Regulation 4601 are to make the regulation prescribe the manner of serving all of the notices the Board is required to serve under the Act, require that all of the notices be served in the manner prescribed for service of a notice under BPC section 22971.5, and generally ensure that the regulation is consistent with BPC section 22971.5. The Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

The text of the proposed amendments to Regulation 4601 is slightly different than the text that the Board approved on June 26, 2012. The original text provided that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law.” However, section 22971.5 was added to the BPC after the Board’s adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised the approved text of the amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board’s proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board’s proposed amendments provide that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5.”

#### *Amendments to Regulations 4603 through 4605*

Regulations 4603 through 4605 provide that a suspension period may be reduced to “0 days, 10 days, or 20 days” when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10 days would be appropriate. The intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to add a 5-day suspension period to the regulations to specifically give the Board additional flexibility to reduce suspensions based upon staff’s belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, the intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to clarify the regulations’ cross-references to statutes that require the revocation of retailers’, wholesalers’, distributors’, manufacturers’, and importers’ licenses for specified violations of the Act; and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

The proposed amendments also update the reference notes to Regulations 4601, 4603, 4604, and 4605 to better reflect the contents of each reference note’s regulation.

#### *Business Taxes Committee Process*

The Board approved the amendments to Regulation 4601, 4603, 4604, and 4605 (described above) during the Board’s June 26, 2012, Business Taxes Committee meeting, but, at the conclusion of the meeting, the Board voted to postpone proposing the amendments to

Regulations 4601, 4603, 4604, and 4605 while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other provisions of the Act. During the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 at this time, and the Board did not decide to propose to adopt a new regulation at that time.

The Board has performed an evaluation of whether the proposed amendments to Regulations 4601, 4603, 4604, and 4605 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 4601 is the only state regulation prescribing the manner for serving a notice issued under the Act and Regulations 4603 through 4605 are the only state regulations prescribing the Board's discretion to reduce a suspension imposed under the Act. In addition, there are no comparable federal regulations or statutes to Regulations 4601, 4603, 4604, and 4605.

#### **NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

#### **NO COST OR SAVINGS TO STATE AGENCIES, LOCAL AGENCIES, AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

#### **NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS**

The Board has made an initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 may affect small business.

### **NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES**

The Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

### **RESULTS OF THE ECONOMIC IMPACT ANALYSIS REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)**

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

### **NO SIGNIFICANT EFFECT ON HOUSING COSTS**

Adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant effect on housing costs.

### **DETERMINATION REGARDING ALTERNATIVES**

The Board must determine that no reasonable alternative considered by it or that has been otherwise identified and brought to its attention would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

### **CONTACT PERSONS**

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at

[Bradley.Heller@boe.ca.gov](mailto:Bradley.Heller@boe.ca.gov), or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at [Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

### **WRITTEN COMMENT PERIOD**

The written comment period ends at 10:00 a.m. on June 11, 2013, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulations 4601, 4603, 4604, and 4605 during the June 11, 2013, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605. The Board will only consider written comments received by that time.

### **AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION**

The Board has prepared underscored and strikeout versions of the text of Regulations 4601, 4603, 4604, and 4605 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

### **SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8**

The Board may adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated,

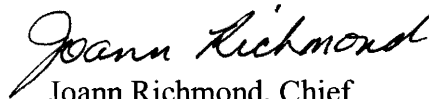
April 19, 2013

available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

#### AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulations 4601, 4603, 4604, and 4605, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

Sincerely,

  
Joann Richmond, Chief  
Board Proceedings Division

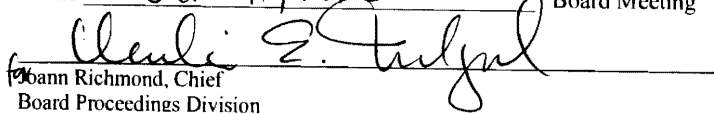
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#### STATE BOARD OF EQUALIZATION



BOARD APPROVED

At the June 11, 2013 Board Meeting

  
Joann Richmond, Chief  
Board Proceedings Division

## **Initial Statement of Reasons**

### **Adoption of Proposed Amendments to California Code of Regulations, Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

#### **SPECIFIC PURPOSE AND NECESSITY**

##### Current Law

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Cigarette and Tobacco Products Licensing Act (Act) to division 8.6 (commencing with section 22970) of the Business and Professions Code (BPC). As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the State Board of Equalization (Board) pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted California Code of Regulations, title 18, sections (Regulations) 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, and 4601, *Service of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to and serve such notice on a person that has been issued a citation for a violation of the Act. Regulation 4601 currently provides that:

The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub-post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be



deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*, to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

### Specific Purpose, Necessity, and Benefits of the Proposed Amendments

#### *Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, to specifically address the problem, Board staff prepared Formal Issue Paper 12-007, which recommended that the Board

1. Amend Regulation 4601 so that it applies to all of the notices the Board is required to serve under the Act and requires that all of the notices be served in the manner provided for in RTC section 30206 for the service of a notice of determination; and
2. Shorten the name of Regulation 4601 to “Service of a Notice” to reflect the expanded application of the regulation’s provisions.

The Board considered Formal Issue Paper 12-007 during its Business Taxes Committee meeting on June 26, 2012. The Board agreed with staff's recommendations and unanimously voted to propose the adoption of staff's recommended amendments to Regulation 4601 because the Board determined that the amendments were reasonably necessary to expressly prescribe the manner in which the Board shall serve all the notices required to be served under the Act and make the name of Regulation 4601 consistent with its amended contents.

The text of the proposed amendments to Regulation 4601 is slightly different than the text of staff's recommended amendments to Regulation 4601, as shown in exhibit 3 to Formal Issue Paper 12-007. The text shown in exhibit 3 to the issue paper provided that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law." However, section 22971.5 was added to the BPC after the Board's adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised staff's recommended amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board's proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board's proposed amendments provide that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5." In addition, the Board has proposed to amend Regulation 4601's reference note so that it only refers to BPC section 22971.5.

The Board has determined that the proposed amendments to Regulation 4601 are reasonably necessary to expressly prescribe the manner in which the Board shall serve all the notices required to be served under the Act and make the name of Regulation 4601 and the regulation's reference note consistent with the regulation's amended contents. The Board also determined that the proposed amendments to Regulation 4601 are reasonably necessary to specifically address the problem created by the regulation's lack of guidance regarding the service of notices, other than Warning Notices and Notices of Violation, that the Board is required to serve under the Act, and the Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

#### *Amendments to Regulations 4603 through 4605*

Regulations 4603 through 4605 provide that a suspension period may be reduced to "0 days, 10 days, or 20 days" when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10

days would be appropriate. Therefore, Board staff initially recommended that the Board amend Regulations 4603 and 4605 to provide for the reduction of a suspension within a range of between 1 and 20 days to give the Board more flexibility. However, some interested parties objected to staff's initial recommendation because they felt that shorter suspension periods, such as 1 day, would not be sufficient to deter violations of the Act and would be difficult for the Board to enforce.

As a result, Board staff alternatively recommended that the Board amend Regulations 4603 through 4605 to provide for the reduction of a suspension to "5 days," in addition to 0 days, 10 days, and 20 days. The alternative recommendation was based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period.

Board staff presented both of its alternative amendments to Regulations 4603 through 4605 to the Board as part of Formal Issue Paper 12-007. Mr. Steven Alari, representing SEIU Local 1000, appeared at the Board's June 26, 2012, Business Taxes Committee meeting and generally supported staff's recommendation adding a 5-day suspension period to all three regulations. As a result, the Board unanimously voted to propose adding a 5-day suspension period to the regulations because the Board determined that the amendments were reasonably necessary to specifically give the Board additional flexibility to reduce suspensions. The Board also determined that the amendments to Regulations 4603 through 4605 are necessary to address the problem that currently exists when a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of 5 days would be more appropriate, and the Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, Regulation 4603 applies to retailers, and subdivision (f) of Regulation 4603 provides that a retailer's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC section 22978.6. However, section 22978.6 provides for the revocation of distributors' and wholesalers' licenses, not retailers' licenses. Also, subdivision (f) of Regulation 4603 does not refer to BPC sections 22974.3, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), and these subdivisions do require the revocation of retailers' licenses for specified violations of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the reference to BPC section 22978.6 from subdivision (f) of Regulation 4603, adding references to BPC sections 22974.3, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), to subdivision (f) of Regulation 4603, and adding a reference to BPC section 22980.3, subdivision (d), to Regulation 4603's reference note.

Further, Regulation 4604 applies to wholesalers and distributors, and subdivision (f) of Regulation 4604 provides that a wholesaler's or distributor's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC section 22974.4. However, section 22974.4 provides for the revocation of retailers' licenses, not wholesalers' and distributors' licenses. Also, subdivision (f) of

Regulation 4604 does not refer to BPC sections 22978.2, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), and these subdivisions do require the revocation of wholesalers' and distributors' licenses for specified violations of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the references to BPC section 22974.4 from subdivision (f) of Regulation 4604 and Regulation 4064's reference note, adding references to BPC sections 22978.2, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), to subdivision (f) of Regulation 4604, and adding a reference to BPC section 22980.3, subdivisions (a)(2) and (d), to Regulation 4604's reference note. Board staff also recommended moving the reference to BPC section 22978.7 in Regulation 4604's reference note so that all of the statutory references in the reference note are in numerical order.

Furthermore, Regulation 4605 applies to manufacturers and importers, and subdivision (e) of Regulation 4605 provides that a manufacturer's or importer's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC sections 22974.4 and 22978.6. However, BPC sections 22974.4 and 22978.6 do not apply to the revocation of manufacturers' and importers' licenses. Also, subdivision (e) of Regulation 4605 does not refer to BPC section 22980.3, subdivision (d), and this subdivision does require the revocation of manufacturers' and importers' licenses for a specified violation of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the references to BPC sections 22974.4 and 22978.6 from subdivision (e) of Regulation 4605, adding a reference to BPC section 22980.3, subdivision (d), to subdivision (e) of Regulation 4605, and adding a reference to BPC section 22980.3, subdivisions (a)(2) and (d), to Regulation 4605's reference note. Board staff also recommended deleting the reference to BPC section 22978.7 from Regulation 4605's reference note because that section does not apply to manufacturers and importers and is not being interpreted, implemented, or made specific by the regulation, and moving the references to BPC sections 22979.4 and 22979.6, subdivision (c), in Regulation 4605's reference note so that all of the statutory references in the reference note are in numerical order.

Therefore, during the June 26, 2012, Business Taxes Committee meeting, the Board also unanimously voted to propose all of these additional amendments to the references to the BPC in Regulations 4603 through 4605 because the Board determined that the amendments were reasonably necessary to ensure that each regulation accurately cross-references the applicable revocation statutes and each regulation's reference note only refers to statutes that are being implemented, interpreted, or made specific by such regulation. The Board also determined that the additional amendments to Regulations 4603 through 4605 are necessary to address the confusion created by the regulations' current statutory references, and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

Finally, at the conclusion of the Board's June 26, 2012, Business Taxes Committee meeting, the Board voted to postpone proposing the amendments to Regulations 4601, 4603, 4604, and 4605 described above while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other

provisions of the Act. However, during the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 described above, and the Board did not decide to propose to adopt a new regulation at that time.

The proposed amendments to Regulations 4601, 4603, 4604, and 4605 were not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulations 4601, 4603, 4604, and 4605.

## DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 12-007, the exhibit to the issue paper, and the comments made during the Board's discussion of the issue paper during its June 26, 2012, Business Taxes Committee meeting in deciding to propose the amendments to Regulations 4601, 4603, 4604, and 4605 described above.

## ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed amendments at this time because the Board determined that the proposed amendments are reasonably necessary for the reasons set forth above.

The Board also considered whether to amend Regulations 4603 through 4605 to provide for the reduction of a suspension within a range of between 1 and 20 days or to provide for the reduction of a suspension to "5 days," in addition to 0 days, 10 days, and 20 days. The Board decided that the latter alternative was more appropriate based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board rejected the former alternative based upon the concern that shorter suspension periods, such as 1 day, might not be sufficient to deter violations of the Act and would be difficult for the Board to enforce. The Board did not reject any other reasonable alternatives to the proposed amendments.

There was no information presented to the Board to indicate that the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will have any adverse impact on small business. Also, no reasonable alternatives have been identified and brought to the Board's attention that would be less burdensome and equally effective in achieving the purposes of the proposed amendments or that would lessen any adverse impact the proposed amendments may have on small business. Therefore, the Board did not reject any alternatives to the proposed amendments that would be less burdensome and equally effective in achieving the purposes of the proposed amendments or that would lessen any adverse impact the proposed amendments may have on small business.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2,  
SUBDIVISION (b)(6) AND ECONOMIC IMPACT ANALYSIS REQUIRED BY  
GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The proposed amendments to Regulation 4601 simply require notices issued under the Act to be served in the manner provided by BPC section 22971.5 for the service of notices under the Act. As such, the amendments merely make the regulation consistent with the applicable statute regarding the service of such notices.

The Board already has discretion to reduce a suspension period to 0 days, 10 days, or 20 days when mitigating factors are present. The proposed amendments to Regulations 4603 through 4605 will also permit the Board to reduce a suspension period to 5 days when mitigating factors are present. The Board intends to use the 5-day suspension period in those situations where the Board would currently impose a 10-day suspension, but the Board determines that a 10-day suspension would be too harsh, and the Board does not intend to use the 5-day suspension period where the Board would currently reduce a suspension period to 0 days. Therefore, the Board anticipates that some persons will benefit from the proposed amendments by having their suspensions reduced to 5 days instead of 10 days.

Therefore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

In addition, Regulations 4601, 4603, 4604, and 4605 do not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant adverse economic impact on business.

The proposed amendments may affect small business.

**Text of Proposed Amendments to  
California Code of Regulations, Title 18, Sections  
4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*,  
4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and  
4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

**4601. Service of a Notice of Violation or Warning Notice.**

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5. The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22971.5~~22974.7~~, ~~22978.7~~ and ~~22979.7~~, Business and Professions Code.

**4603. Penalties for Licensed or Unlicensed Retailers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).
- (2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, ~~22978.6~~, or 22980.3, subdivision (a)(2) or subdivision (d).



Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22973(a)(5), 22974, 22974.3, 22974.4, 22974.7, 22980.1(c), (d), (e) and (g), 22980(b), 22980.2(a) and 22980.3(a)(2) and (d), Business and Professions Code.

#### **4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).
- (2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).
- (3) Business and Professions Code section 22978.5, subdivision (b) (distributor's or wholesaler's failure to retain sales records).
- (4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

- (1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).
- (2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4~~22978.2~~, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, 22977(a)(5), 22978.1, 22978.2, ~~22978.7~~, 22978.5(b), 22978.7, 22979.7, 22980(b), 22980.1(b), (c), (d), (e), (f) and (g), ~~and 22980.2(a) and 22980.3(a)(2) and (d)~~, Business and Professions Code.

#### **4605. Penalties for Licensed or Unlicensed Manufacturers and Importers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).
- (2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).
- (3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).
- (4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).
- (6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

(b) A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)) shall result in a 20-day suspension.

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

(d) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, ~~22978.7, 22979.4~~, 22979(b)(1), ~~22979.4~~, 22979.5(b), 22979.6(c), 22979.7, 22980.1(a), (e) and (f), 22980.2(a), and 22980.3(a)(2) and (d)~~22979.6(e)~~, Business and Professions Code.

## Regulation History

### **Type of Regulations: Cigarette and Tobacco Products Licensing Act**

Regulations: 4601, 4603, 4604, and 4605

Titles: *Service of a Notice of Violation or Warning Notice*  
*Penalties for Licensed or Unlicensed Retailers*  
*Penalties for Licensed or Unlicensed Wholesalers and Distributors*  
*Penalties for Licensed or Unlicensed Manufacturers and Importers*

**Preparation:** Bradley Heller

**Legal Contact:** Bradley Heller

The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) to be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code (BPC) section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

### **History of Proposed Regulation:**


June 11, 2013	Public Hearing
April 19, 2013	OAL publication date; 45-day public comment period begins; Interested Parties mailing
April 9, 2013	Notice to OAL
January 15, 2013	Business Tax Committee, Board Authorized Publication (Vote 5-0)

Sponsor:	NA
Support:	NA
Oppose:	NA

## Statement of Compliance

The State Board of Equalization, in process of adopting Special Taxes Regulations 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*, did comply with the provision of Government Code section 11346.4(a)(1) through (4). A notice to interested parties was mailed on April 19, 2013, 53 days prior to the public hearing.

April 29, 2013

A handwritten signature in black ink, appearing to read "Richard Bennion", written over a horizontal line.

Richard Bennion  
Regulations Coordinator  
State Board of Equalization

1       BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION  
2                   450 N STREET  
3                   SACRAMENTO, CALIFORNIA  
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8                   REPORTER'S TRANSCRIPT  
9                   JUNE 11, 2013  
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12                   ITEM F2  
13       PROPOSED ADOPTION OF AMENDMENTS TO CIGARETTE AND  
14                   TOBACCO PRODUCTS LICENSING ACT  
15                   REGULATIONS 4601, 4603, 4604 AND 4605  
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27                   REPORTED BY: Kathleen Skidgel  
28                   CSR NO. 9039

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P R E S E N T

For the Board of Equalization:	Jerome E. Horton Chairman
	Michelle Steel Vice-Chairwoman
	Betty T. Yee Member
	George Runner Member
	Marcy Jo Mandel Appearing for John Chiang, State Controller (per Government Code Section 7.9)
	Joann Richmond Chief, Board Proceedings Division
For Board of Equalization Staff:	Bradley Heller Legal Department

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1 450 N STREET  
2 SACRAMENTO, CALIFORNIA  
3 JUNE 11, 2013

4 ---OOO---

5 MR. HORTON: Ms. Richmond.

6 MS. RICHMOND: Our next item is F2,  
7 Proposed Adoption of Amendments to Cigarette and  
8 Tobacco Products Licensing Act Regulations 4601,  
9 Service of a Notice of Violation or Warning Notice,  
10 4603, Penalties for Licensed or Unlicensed  
11 Retailers, 4604, Penalties for Licensed or  
12 Unlicensed wholesalers and Distributors, and 4605,  
13 Penalties for Licensed or Unlicensed Manufacturers  
14 and Importers.

15 MR. HORTON: Thank you.

16 Members, we would ask staff to make  
17 presentation on this item.

18 welcome, Mr. Heller.

19 MR. HELLER: Thank you Chairman Horton,  
20 Members of the Board.

21 I'm Bradley Heller from the Board's Legal  
22 Department, and I'm here to request that the Board  
23 vote to adopt proposed amendments to cigarette  
24 and -- excuse me, to Cigarette and Tobacco Products  
25 Licensing Act Regulations 4601, 4603, 4604 and 4605.



26           The amendments to regulation 4601 prescribe  
27   the manner of serving all notices required under the  
28   act. The proposed amendments to Regulations 4603

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1   through 4605 provide the Board with additional  
2   discretion to reduce a person's suspension for a  
3   violation of the act to five days when mit -- when  
4   mitigating factors are present.

5           I can answer any questions the Board  
6   Members may have.

7           MR. HORTON: Thank you.

8           Member Steel, please.

9           MS. STEEL: When we, uh, did this, uh, from  
10   zero to ten days and twenty days to five days means  
11   that ten days was too severe to ask tax -- taxpayer  
12   to close down their businesses.

13           So I want to look at the stats that five  
14   days -- I hope that zero days not going to fall into  
15   five days. So I really want to look at closely. So  
16   next time when you come out, uh, come to the Board  
17   hearing, I want to look at the numbers that how many  
18   people really got suspended for five days instead of  
19   zero days and I just want to compare those notes.

20           MR. HELLER: Ms. Steel, I'll make sure the  
21   Department tracks --

22           MS. STEEL: Thank you.

23           MR. HELLER: -- the implementation of  
                            Page 4

24 that.

25 MS. STEEL: Thank you.

26 MR. HORTON: Thank you.

27 Um, further discussion, Members?

28 So how did you come up with these numbers,

4

1 Mr. Heller?

2 MR. HELLER: Really the five is just kind  
3 of the in between the ten and the zero --

4 MR. HORTON: Oh. Thank you very much.

5 MR. HELLER: -- as Ms. Steel was just  
6 explaining.

7 MR. HORTON: Is there a motion, Members?

8 MS. STEEL: So move.

9 MR. HORTON: Moved by Member Steel, second  
10 by Member Runner.

11 Without objection, Members, such will be  
12 the order.

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1 REPORTER'S CERTIFICATE

2

3 State of California )  
4 ) ss  
5 County of Sacramento )

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7 I, KATHLEEN SKIDGEL, Hearing Reporter for  
8 the California State Board of Equalization certify  
9 that on June 11, 2013 I recorded verbatim, in  
10 shorthand, to the best of my ability, the  
11 proceedings in the above-entitled hearing; that I  
12 transcribed the shorthand writing into typewriting;  
13 and that the preceding pages 1 through 5 constitute  
14 a complete and accurate transcription of the  
15 shorthand writing.

16

17 Dated: June 14, 2013

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KATHLEEN SKIDGEL, CSR #9039

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Hearing Reporter

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**2013 MINUTES OF THE STATE BOARD OF EQUALIZATION****Tuesday, June 11, 2013****PUBLIC HEARINGS****F2 PROPOSED ADOPTION OF AMENDMENTS TO CIGARETTE AND TOBACCO PRODUCTS LICENSING ACT (ACT) REGULATIONS 4601, 4603, 4604 AND 4605**

Bradley Heller, Tax Counsel, Tax and Fee Programs Division, Legal Department, made introductory remarks regarding staff's request for adoption of proposed amendments to Cigarette and Tobacco Products Licensing Act (Act) Regulations 4601, *Service of a Notice of Violation or Warning Notice*; 4603, *Penalties for Licensed or Unlicensed Retailers*; 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*; and, 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*; to provide for the service of all notices under the Act and the reduction of suspensions to five days when warranted (Exhibit 6.3).

Speakers were invited to address the Board, but there were none.

Action: Upon motion of Ms. Steel, seconded by Mr. Runner and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee, Mr. Runner and Ms. Mandel voting yes, the Board adopted the amendments to Cigarette and Tobacco Products Licensing Act (Act) Regulations 4601, 4603, 4604 and 4605 as recommended by staff.

Ms. Steel requested a report regarding staff's use of the new discretion to reduce suspensions to 5 days, after the proposed amendments to Regulations 4603-4605 are effective and implemented, to make sure that staff is using the discretion to help taxpayers by reducing what would otherwise be 10-day suspensions to 5-day suspensions, when a 10-day suspension seems to harsh, and staff is not using the discretion to increase what would otherwise be 0-day suspensions to 5-day suspensions.

**F3 Proposed Adoption of Amendments to Property Tax Rule 462.040, *Change in Ownership – Joint Tenancies***

Bradley Heller, Tax Counsel, Tax and Fee Programs Division, Legal Department, made introductory remarks regarding staff's request for adoption of amendments to Property Tax Rule 462.040, *Change in Ownership – Joint Tenancies*, to make the rule consistent with and clarify current law regarding transactions involving joint tenancies (Exhibit 6.4).

Speakers: Janet Lewis, Supervising Real Property Appraiser, Sacramento County Assessor's Office  
Barbara Edginton, Manager, San Luis Obispo County Assessor's Office

Action: Upon motion of Ms. Yee, seconded by Ms. Steel and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee, Mr. Runner and Ms. Mandel voting yes, the Board adopted the amendments to Property Tax Rule 462.040 as recommended by staff.

Ms. Yee thanked Ms. Edginton for her work on this regulation.



STATE OF CALIFORNIA

**STATE BOARD OF EQUALIZATION**

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Fourth District, Los Angeles

JOHN CHIANG  
State Controller

CYNTHIA BRIDGES  
Executive Director

**April 19, 2013**

**To Interested Parties:**

**Notice of Proposed Regulatory Action  
by the  
State Board of Equalization**

**Proposes to Amendments to California Code of Regulations, Title 18,  
Sections 4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for  
Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties  
for Licensed or Unlicensed Manufacturers and Importers***

**NOTICE IS HEREBY GIVEN**

The State Board of Equalization (Board), pursuant to the authority vested in it by Business and Professions Code (BPC) section 22971.2, proposes to adopt amendments to California Code of Regulations, title 18, sections (Regulations) 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*. The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) (div. 8.6 (commencing with § 22970) of the BPC) to be served personally or by mail in the manner prescribed for service of a notice under BPC section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

## **PUBLIC HEARING**

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 11, 2013. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on June 11, 2013. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605.

## **AUTHORITY**

BPC section 22971.2.

## **REFERENCE**

Regulation 4601:	BPC section 22971.5
Regulation 4603:	BPC sections 22973, 22974, 22974.3, 22974.4, 22974.7, 22980, 22980.1, 22980.2, and 22980.3
Regulation 4604:	BPC sections 22974.7, 22977, 22978.1, 22978.2, 22978.5, 22978.7, 22979.7, 22980, 22980.1, 22980.2, and 22980.3
Regulation 4605:	BPC sections 22974.7, 22979, 22979.4, 22979.5, 22979.6, 22979.7, 22980.1, 22980.2, and 22980.3

## **INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW**

### Current Law

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Act to the BPC. As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the

Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the Board pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted Regulation 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to a person that has been issued a citation for a violation of the Act, and the Board adopted Regulation 4601 to prescribe the manner in which a Notice of Violation or Warning Notice shall be served. The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, 4604, and 4605 to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

Effect, Objectives, and Benefits of the Proposed Amendments to Regulations 4601, 4603, 4604, and 4605

#### *Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, the intent and objectives of the proposed amendments to Regulation 4601 are to make the regulation prescribe the manner of serving all of the notices the Board is required to serve under the Act, require that all of the notices be served in the manner prescribed for service of a notice under BPC section 22971.5, and generally ensure that the regulation is consistent with BPC section 22971.5. The Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.



The text of the proposed amendments to Regulation 4601 is slightly different than the text that the Board approved on June 26, 2012. The original text provided that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law.” However, section 22971.5 was added to the BPC after the Board’s adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised the approved text of the amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board’s proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board’s proposed amendments provide that “Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5.”

#### *Amendments to Regulations 4603 through 4605*

Regulations 4603 through 4605 provide that a suspension period may be reduced to “0 days, 10 days, or 20 days” when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10 days would be appropriate. The intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to add a 5-day suspension period to the regulations to specifically give the Board additional flexibility to reduce suspensions based upon staff’s belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, the intent and objectives of the proposed amendments to Regulations 4603 through 4605 are to clarify the regulations’ cross-references to statutes that require the revocation of retailers’, wholesalers’, distributors’, manufacturers’, and importers’ licenses for specified violations of the Act; and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

The proposed amendments also update the reference notes to Regulations 4601, 4603, 4604, and 4605 to better reflect the contents of each reference note’s regulation.

#### *Business Taxes Committee Process*

The Board approved the amendments to Regulation 4601, 4603, 4604, and 4605 (described above) during the Board’s June 26, 2012, Business Taxes Committee meeting, but, at the conclusion of the meeting, the Board voted to postpone proposing the amendments to

Regulations 4601, 4603, 4604, and 4605 while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other provisions of the Act. During the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 at this time, and the Board did not decide to propose to adopt a new regulation at that time.

The Board has performed an evaluation of whether the proposed amendments to Regulations 4601, 4603, 4604, and 4605 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 4601 is the only state regulation prescribing the manner for serving a notice issued under the Act and Regulations 4603 through 4605 are the only state regulations prescribing the Board's discretion to reduce a suspension imposed under the Act. In addition, there are no comparable federal regulations or statutes to Regulations 4601, 4603, 4604, and 4605.

#### **NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

#### **NO COST OR SAVINGS TO STATE AGENCIES, LOCAL AGENCIES, AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

#### **NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS**

The Board has made an initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 may affect small business.

### **NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES**

The Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

### **RESULTS OF THE ECONOMIC IMPACT ANALYSIS REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)**

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

### **NO SIGNIFICANT EFFECT ON HOUSING COSTS**

Adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant effect on housing costs.

### **DETERMINATION REGARDING ALTERNATIVES**

The Board must determine that no reasonable alternative considered by it or that has been otherwise identified and brought to its attention would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

### **CONTACT PERSONS**

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at

[Bradley.Heller@boe.ca.gov](mailto:Bradley.Heller@boe.ca.gov), or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at [Richard.Bennion@boe.ca.gov](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

### **WRITTEN COMMENT PERIOD**

The written comment period ends at 10:00 a.m. on June 11, 2013, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulations 4601, 4603, 4604, and 4605 during the June 11, 2013, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605. The Board will only consider written comments received by that time.

### **AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION**

The Board has prepared underscored and strikeout versions of the text of Regulations 4601, 4603, 4604, and 4605 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

### **SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8**

The Board may adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated,

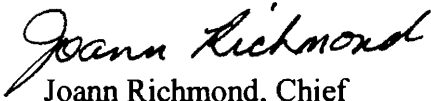
April 19, 2013

available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

#### **AVAILABILITY OF FINAL STATEMENT OF REASONS**

If the Board adopts the proposed amendments to Regulations 4601, 4603, 4604, and 4605, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

Sincerely,

  
Joann Richmond, Chief  
Board Proceedings Division

JR:reb

## **Initial Statement of Reasons**

### **Adoption of Proposed Amendments to California Code of Regulations, Title 18, Sections 4601, *Service of a Notice of Violation or Warning Notice*, 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

#### **SPECIFIC PURPOSE AND NECESSITY**

##### **Current Law**

On October 12, 2003, the State of California enacted Assembly Bill No. (AB) 71 (Stats. 2003, ch. 890 (Horton)), and section 1 of AB 71 added the Cigarette and Tobacco Products Licensing Act (Act) to division 8.6 (commencing with section 22970) of the Business and Professions Code (BPC). As originally enacted, the Act imposed licensing requirements on all retailers, wholesalers, and distributors of cigarettes and tobacco products and all manufacturers and importers of cigarettes. In 2006, the State of California enacted AB 1749 (Stats. 2006, ch. 501 (Horton)), which added new provisions to the Act that imposed the same licensing requirements on manufacturers and importers of tobacco products as were previously imposed on manufacturers and importers of cigarettes.

The Act is administered by the State Board of Equalization (Board) pursuant to BPC section 22971.2, and, in 2006, the Board adopted a number of regulations to implement, interpret, and make specific the Act's licensing requirements. As relevant here, the Board adopted California Code of Regulations, title 18, sections (Regulations) 4600, *Issuance and Contents of a Notice of Violation or Warning Notice*, and 4601, *Service of a Notice of Violation or Warning Notice*, to require the Board to issue a Notice of Violation or Warning Notice to and serve such notice on a person that has been issued a citation for a violation of the Act. Regulation 4601 currently provides that:

The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub-post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be

deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

The text of Regulation 4601 is based upon the text of Revenue and Taxation Code (RTC) section 30206, which provides for the service of a notice of determination issued under the Cigarette and Tobacco Products Tax Law (RTC § 30001 et seq.).

The Board also adopted Regulations 4603, *Penalties for Licensed or Unlicensed Retailers*, 4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and 4605, *Penalties for Licensed and Unlicensed Manufacturers and Importers*, to provide for the issuance of a Warning Notice, or the imposition of a 10-day, 20-day, or 30-day suspension, or the revocation of a license and the imposition of a fine for specified violations of the Act; and to provide for the reduction in the length of a suspension and changing a revocation to a 30-day suspension, when mitigating factors warrant. As relevant here, the second and third sentences in subdivision (f) of Regulations 4603 and 4604 and subdivision (e) of Regulation 4605 all currently provide that:

If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2).

### Specific Purpose, Necessity, and Benefits of the Proposed Amendments

#### *Amendments to Regulation 4601*

A person has the right to appeal when the Board has alleged that the person violated the Act. When timely appeals are made, the Board is required to issue notices under Regulations 4700, *Appeal – Special Taxes and Fees Division*, 4701, *Appeal – Appeals Division*, and 4702, *Appeal – Board Hearing*. However, Regulation 4601 only prescribes the manner of serving a Notice of Violation or Warning Notice, and there is no regulation expressly prescribing the manner in which the Board shall serve other notices required to be served under the Act, such as the notices required by Regulations 4700 through 4702. Therefore, to specifically address the problem, Board staff prepared Formal Issue Paper 12-007, which recommended that the Board

1. Amend Regulation 4601 so that it applies to all of the notices the Board is required to serve under the Act and requires that all of the notices be served in the manner provided for in RTC section 30206 for the service of a notice of determination; and
2. Shorten the name of Regulation 4601 to “Service of a Notice” to reflect the expanded application of the regulation’s provisions.

The Board considered Formal Issue Paper 12-007 during its Business Taxes Committee meeting on June 26, 2012. The Board agreed with staff's recommendations and unanimously voted to propose the adoption of staff's recommended amendments to Regulation 4601 because the Board determined that the amendments were reasonably necessary to expressly prescribe the manner in which the Board shall serve all the notices required to be served under the Act and make the name of Regulation 4601 consistent with its amended contents.

The text of the proposed amendments to Regulation 4601 is slightly different than the text of staff's recommended amendments to Regulation 4601, as shown in exhibit 3 to Formal Issue Paper 12-007. The text shown in exhibit 3 to the issue paper provided that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice of determination under Revenue and Taxation Code section 30206 of the Cigarette and Tobacco Products Tax Law." However, section 22971.5 was added to the BPC after the Board's adoption of Regulation 4601 to prescribe the manner for serving any notice required under the Act. Therefore, the Board revised staff's recommended amendments to Regulation 4601, prior to beginning the formal rulemaking process, in order to make the text of the Board's proposed amendments to Regulation 4601 fully consistent with the provisions of BPC section 22971.5, which are substantially similar to the provisions of RTC section 30206. The Board's proposed amendments provide that "Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5." In addition, the Board has proposed to amend Regulation 4601's reference note so that it only refers to BPC section 22971.5.

The Board has determined that the proposed amendments to Regulation 4601 are reasonably necessary to expressly prescribe the manner in which the Board shall serve all the notices required to be served under the Act and make the name of Regulation 4601 and the regulation's reference note consistent with the regulation's amended contents. The Board also determined that the proposed amendments to Regulation 4601 are reasonably necessary to specifically address the problem created by the regulation's lack of guidance regarding the service of notices, other than Warning Notices and Notices of Violation, that the Board is required to serve under the Act, and the Board anticipates that the public, including regulated persons, will benefit from the increased openness and transparency regarding the procedures for the service of all notices required under the Act.

#### *Amendments to Regulations 4603 through 4605*

Regulations 4603 through 4605 provide that a suspension period may be reduced to "0 days, 10 days, or 20 days" when mitigating factors warrant, but the regulations do not give the Board sufficient flexibility to reduce suspensions because there are situations where a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of more than 0 days and less than 10



days would be appropriate. Therefore, Board staff initially recommended that the Board amend Regulations 4603 and 4605 to provide for the reduction of a suspension within a range of between 1 and 20 days to give the Board more flexibility. However, some interested parties objected to staff's initial recommendation because they felt that shorter suspension periods, such as 1 day, would not be sufficient to deter violations of the Act and would be difficult for the Board to enforce.

As a result, Board staff alternatively recommended that the Board amend Regulations 4603 through 4605 to provide for the reduction of a suspension to "5 days," in addition to 0 days, 10 days, and 20 days. The alternative recommendation was based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period.

Board staff presented both of its alternative amendments to Regulations 4603 through 4605 to the Board as part of Formal Issue Paper 12-007. Mr. Steven Alari, representing SEIU Local 1000, appeared at the Board's June 26, 2012, Business Taxes Committee meeting and generally supported staff's recommendation adding a 5-day suspension period to all three regulations. As a result, the Board unanimously voted to propose adding a 5-day suspension period to the regulations because the Board determined that the amendments were reasonably necessary to specifically give the Board additional flexibility to reduce suspensions. The Board also determined that the amendments to Regulations 4603 through 4605 are necessary to address the problem that currently exists when a 10-day suspension is too harsh, a 0-day suspension would not be sufficient to deter violations of the Act, and a suspension period of 5 days would be more appropriate, and the Board anticipates that the Board and regulated persons will benefit by the establishment of a fair, 5-day suspension period to address such situations.

In addition, Regulation 4603 applies to retailers, and subdivision (f) of Regulation 4603 provides that a retailer's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC section 22978.6. However, section 22978.6 provides for the revocation of distributors' and wholesalers' licenses, not retailers' licenses. Also, subdivision (f) of Regulation 4603 does not refer to BPC sections 22974.3, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), and these subdivisions do require the revocation of retailers' licenses for specified violations of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the reference to BPC section 22978.6 from subdivision (f) of Regulation 4603, adding references to BPC sections 22974.3, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), to subdivision (f) of Regulation 4603, and adding a reference to BPC section 22980.3, subdivision (d), to Regulation 4603's reference note.

Further, Regulation 4604 applies to wholesalers and distributors, and subdivision (f) of Regulation 4604 provides that a wholesaler's or distributor's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC section 22974.4. However, section 22974.4 provides for the revocation of retailers' licenses, not wholesalers' and distributors' licenses. Also, subdivision (f) of

Regulation 4604 does not refer to BPC sections 22978.2, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), and these subdivisions do require the revocation of wholesalers' and distributors' licenses for specified violations of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the references to BPC section 22974.4 from subdivision (f) of Regulation 4604 and Regulation 4064's reference note, adding references to BPC sections 22978.2, subdivisions (a)(2) and (a)(4), and 22980.3, subdivision (d), to subdivision (f) of Regulation 4604, and adding a reference to BPC section 22980.3, subdivisions (a)(2) and (d), to Regulation 4604's reference note. Board staff also recommended moving the reference to BPC section 22978.7 in Regulation 4604's reference note so that all of the statutory references in the reference note are in numerical order.

Furthermore, Regulation 4605 applies to manufacturers and importers, and subdivision (e) of Regulation 4605 provides that a manufacturer's or importer's revocation penalty will not be reduced to a 30-day suspension if revocation is required by specified BPC sections, including BPC sections 22974.4 and 22978.6. However, BPC sections 22974.4 and 22978.6 do not apply to the revocation of manufacturers' and importers' licenses. Also, subdivision (e) of Regulation 4605 does not refer to BPC section 22980.3, subdivision (d), and this subdivision does require the revocation of manufacturers' and importers' licenses for a specified violation of the Act. Therefore, in Formal Issue Paper 12-007, Board staff recommended deleting the references to BPC sections 22974.4 and 22978.6 from subdivision (e) of Regulation 4605, adding a reference to BPC section 22980.3, subdivision (d), to subdivision (e) of Regulation 4605, and adding a reference to BPC section 22980.3, subdivisions (a)(2) and (d), to Regulation 4605's reference note. Board staff also recommended deleting the reference to BPC section 22978.7 from Regulation 4605's reference note because that section does not apply to manufacturers and importers and is not being interpreted, implemented, or made specific by the regulation, and moving the references to BPC sections 22979.4 and 22979.6, subdivision (c), in Regulation 4605's reference note so that all of the statutory references in the reference note are in numerical order.

Therefore, during the June 26, 2012, Business Taxes Committee meeting, the Board also unanimously voted to propose all of these additional amendments to the references to the BPC in Regulations 4603 through 4605 because the Board determined that the amendments were reasonably necessary to ensure that each regulation accurately cross-references the applicable revocation statutes and each regulation's reference note only refers to statutes that are being implemented, interpreted, or made specific by such regulation. The Board also determined that the additional amendments to Regulations 4603 through 4605 are necessary to address the confusion created by the regulations' current statutory references, and the Board anticipates that the Board and regulated persons will benefit from the additional clarity provided by the proposed amendments.

Finally, at the conclusion of the Board's June 26, 2012, Business Taxes Committee meeting, the Board voted to postpone proposing the amendments to Regulations 4601, 4603, 4604, and 4605 described above while the Board considered whether to propose the adoption of an additional regulation to implement, interpret, and make specific other

provisions of the Act. However, during the Board's January 15, 2013, Business Taxes Committee meeting, the Board unanimously voted to begin the formal rulemaking process to propose the amendments to Regulations 4601, 4603, 4604, and 4605 described above, and the Board did not decide to propose to adopt a new regulation at that time.

The proposed amendments to Regulations 4601, 4603, 4604, and 4605 were not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulations 4601, 4603, 4604, and 4605.

#### DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 12-007, the exhibit to the issue paper, and the comments made during the Board's discussion of the issue paper during its June 26, 2012, Business Taxes Committee meeting in deciding to propose the amendments to Regulations 4601, 4603, 4604, and 4605 described above.

#### ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulations 4601, 4603, 4604, and 4605 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed amendments at this time because the Board determined that the proposed amendments are reasonably necessary for the reasons set forth above.

The Board also considered whether to amend Regulations 4603 through 4605 to provide for the reduction of a suspension within a range of between 1 and 20 days or to provide for the reduction of a suspension to "5 days," in addition to 0 days, 10 days, and 20 days. The Board decided that the latter alternative was more appropriate based upon staff's belief that a 5-day suspension period is long enough to deter violations of the Act, in some circumstances, and that Board staff has a sufficient amount of time to perform an inspection during a 5-day suspension period. The Board rejected the former alternative based upon the concern that shorter suspension periods, such as 1 day, might not be sufficient to deter violations of the Act and would be difficult for the Board to enforce. The Board did not reject any other reasonable alternatives to the proposed amendments.

There was no information presented to the Board to indicate that the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will have any adverse impact on small business. Also, no reasonable alternatives have been identified and brought to the Board's attention that would be less burdensome and equally effective in achieving the purposes of the proposed amendments or that would lessen any adverse impact the proposed amendments may have on small business. Therefore, the Board did not reject any alternatives to the proposed amendments that would be less burdensome and equally effective in achieving the purposes of the proposed amendments or that would lessen any adverse impact the proposed amendments may have on small business.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2,  
SUBDIVISION (b)(6) AND ECONOMIC IMPACT ANALYSIS REQUIRED BY  
GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The proposed amendments to Regulation 4601 simply require notices issued under the Act to be served in the manner provided by BPC section 22971.5 for the service of notices under the Act. As such, the amendments merely make the regulation consistent with the applicable statute regarding the service of such notices.

The Board already has discretion to reduce a suspension period to 0 days, 10 days, or 20 days when mitigating factors are present. The proposed amendments to Regulations 4603 through 4605 will also permit the Board to reduce a suspension period to 5 days when mitigating factors are present. The Board intends to use the 5-day suspension period in those situations where the Board would currently impose a 10-day suspension, but the Board determines that a 10-day suspension would be too harsh, and the Board does not intend to use the 5-day suspension period where the Board would currently reduce a suspension period to 0 days. Therefore, the Board anticipates that some persons will benefit from the proposed amendments by having their suspensions reduced to 5 days instead of 10 days.

Therefore, the Board has determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

In addition, Regulations 4601, 4603, 4604, and 4605 do not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not affect the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulations 4601, 4603, 4604, and 4605 will not have a significant adverse economic impact on business.

The proposed amendments may affect small business.

**Text of Proposed Amendments to  
California Code of Regulations, Title 18, Sections  
4601, *Service of a Notice of Violation or Warning Notice*,  
4603, *Penalties for Licensed or Unlicensed Retailers*,  
4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*, and  
4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers***

**4601. Service of a Notice of Violation or Warning Notice.**

Any notice issued under the Cigarette and Tobacco Products Licensing Act may be served personally or by mail in the manner prescribed for service of a notice under Business and Professions Code section 22971.5. The Notice of Violation or Warning Notice shall be placed in a sealed envelope, with postage paid, addressed to the licensee or unlicensed person at his or her last known address as it appears in the records of the Board. The giving of notice shall be deemed complete at the time of deposit of the notice at a United States Post Office, a mailbox, sub post office, substation, mail chute, or other facility regularly maintained or provided by the United States Postal Service, without extension of time for any reason. In lieu of mailing, a Notice of Violation may be served personally by delivery to the person to be served and service shall be deemed complete at the time of such delivery. Personal delivery to a corporation may be made by delivery of a notice to any person designated to be served for the corporation with summons and complaint in a civil action, pursuant to the Code of Civil Procedure.

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22971.5~~22974.7~~, ~~22978.7~~ and ~~22979.7~~, Business and Professions Code.

**4603. Penalties for Licensed or Unlicensed Retailers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a retailer has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions shall result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22974 (retailer's failure to retain purchase invoices).
- (2) Business and Professions Code section 22980.1, subdivision (c), (d) or (e) (purchase from unlicensed person or person with suspended or revoked license).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(4) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by an unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions shall result in the issuance of a 20-day suspension:

(1) Business and Professions Code section 22973, subdivision (a)(5) (retailer's false statement on application).

(2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above, shall result in both a 30-day suspension or revocation and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22974.3 (possession of unstamped cigarettes or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during that period.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine shall be determined in accordance with Regulation 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.3 subdivision (a)(2) or subdivision (a)(4), 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22973(a)(5), 22974, 22974.3, 22974.4, 22974.7, 22980.1(c), (d), (e) and (g), 22980(b), 22980.2(a) and 22980.3(a)(2) and (d), Business and Professions Code.

#### **4604. Penalties for Licensed or Unlicensed Wholesalers and Distributors.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a wholesaler or distributor has violated any provision of the Act:

(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22978.1 (distributor's or wholesaler's failure to retain purchase invoices).
- (2) Business and Professions Code section 22978.4, subdivision (c) (distributor's or wholesaler's failure to comply with invoice requirements).
- (3) Business and Professions Code section 22978.5, subdivision (b) (distributor's or wholesaler's failure to retain sales records).
- (4) Business and Professions Code section 22980.1, subdivision (b), (c), (d), (e) (sales to or purchases from unlicensed person or person with suspended or revoked license) or (f) (sales of cigarettes or tobacco products to retailer or wholesaler revoked or suspended until debts are clear).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).

(b) A first offense of a violation of any of the following provisions will result in the issuance of a 20-day suspension:

- (1) Business and Professions Code section 22977, subdivision (a)(5) (distributor's or wholesaler's false statement on application).
- (2) Business and Professions Code section 22980, subdivision (b) (any person's refusal to allow inspection).
- (3) Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)).

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation, and a fine. The fine shall be determined in accordance with Regulation 4607.

(d) A violation of Business and Profession Code section 22978.2 (possession of counterfeit stamped cigarettes by distributors, unstamped cigarettes by wholesalers or untaxed tobacco products) shall result in the following:

(1) Notwithstanding paragraphs (2) and (3) below, a Warning Notice for a first offense when the licensee or unlicensed person has been in business for less than one month and there has been no purchase of new cigarette or tobacco product inventory during the month.

(2) A 10-day suspension for a first offense for a seizure of less than 20 packages of cigarettes, or the equivalent amount of tobacco products based on wholesale cost.

(3) A 20-day suspension for a first offense for a seizure of 20 packages of cigarettes or more, or the equivalent amount of tobacco products based on wholesale cost.

(4) Both a 30-day suspension or revocation and a fine for a second or subsequent offense. The fine will be determined in accordance with section 4607.

(e) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(f) Notwithstanding subdivisions (b) through (e) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section ~~22974.4~~22978.2, subdivision (a)(2) or subdivision (a)(4), 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, 22977(a)(5), 22978.1, 22978.2, ~~22978.7~~, 22978.5(b), 22978.7, 22979.7, 22980(b), 22980.1(b), (c), (d), (e), (f) and (g), ~~and 22980.2(a) and 22980.3(a)(2) and (d)~~, Business and Professions Code.

#### **4605. Penalties for Licensed or Unlicensed Manufacturers and Importers.**

The following penalties shall be assessed in addition to any other civil or criminal penalty provided by law upon a finding that a manufacturer or importer has violated any provision of the Act:



(a) A first offense of a violation of any of the following provisions will result in the issuance of a Warning Notice to the licensee or unlicensed person:

- (1) Business and Professions Code section 22979.4 (importer's failure to retain purchase invoices on premises).
- (2) Business and Professions Code section 22979, subdivision (b)(1) (participating manufacturer's false statement on certification to the Board).
- (3) Business and Professions Code section 22979.5, subdivision (b) (manufacturer's or importer's failure to retain sales records on premises).
- (4) Business and Professions Code section 22980.1, subdivision (a), (e) or (f) (purchases or sales from or to an unlicensed person or person with suspended or revoked license).
- (5) Business and Professions Code section 22980.2, subdivision (a) (sales of cigarettes or tobacco products by unlicensed person or person with suspended or revoked license).
- (6) Business and Professions Code section 22979.6, subdivision (c) (manufacturer's or importer's failure to comply with invoice requirements).

(b) A first offense of a violation of Business and Professions Code section 22980.1, subdivision (g) (purchase of cigarettes to which a stamp may not be affixed in accordance with Rev. & Tax. Code, § 30163, subd. (b)) shall result in a 20-day suspension.

(c) A second or subsequent offense for a violation of the provisions listed in subdivision (a) or (b) above shall result in both a 30-day suspension or revocation and a fine.

(d) In cases involving multiple violations, the violation punishable by the most severe penalty will be used for purposes of determining the penalty assessed.

(e) Notwithstanding subdivisions (b) through (d) above, a reduction in the length of a suspension period may be warranted if mitigating circumstances are present, as set forth in Regulation 4606. If any suspension period is reduced, the redetermined period of suspension shall be 0 days, 5 days, 10 days, or 20 days. The existence of mitigating circumstances may also warrant reducing a revocation penalty to a 30-day suspension, unless revocation is mandated pursuant to Business and Professions Code section 22974.4, 22978.6, or 22980.3, subdivision (a)(2) or subdivision (d).

Note: Authority cited: Section 22971.2, Business and Professions Code. Reference: Sections 22974.7, ~~22978.7, 22979.4, 22979(b)(1), 22979.4, 22979.5(b), 22979.6(c), 22979.7, 22980.1(a), (e) and (f), 22980.2(a), and 22980.3(a)(2) and (d)~~22979.6(e), Business and Professions Code.

## Regulation History

**Type of Regulation:** Special Taxes Regulations

Title: 4601, *Service of a Notice of Violation or Warning Notice*

4603, *Penalties for Licensed or Unlicensed Retailers*

4604, *Penalties for Licensed or Unlicensed Wholesalers and Distributors*

4605, *Penalties for Licensed or Unlicensed Manufacturers and Importers*

**Preparation:** Bradley Heller

**Legal Contact:** Bradley Heller

The proposed amendments to Regulation 4601 provide for all notices issued under the Cigarette and Tobacco Products Licensing Act (Act) (div. 8.6 (commencing with § 22970) of the BPC) to be served personally or by mail in the manner prescribed for service of a notice under BPC section 22971.5. The proposed amendments to Regulations 4603 through 4605 provide the Board with discretion to reduce a person's suspension for a violation of the Act to "5 days," in addition to the Board's current discretion to reduce a person's suspension to 0 days, 10 days, and 20 days, when mitigating factors are present. The proposed amendments clarify cross-references to the BPC in Regulations 4603 through 4605 and make all four regulations' reference notes consistent with the content of their respective regulations.

### History of Proposed Regulation:

June 11, 2013	Public Hearing
April 19, 2013	OAL publication date; 45-day public comment period begins; Interested Parties mailing
April 9, 2013	Notice to OAL
January 15, 2013	Business Tax Committee, Board Authorized Publication (Vote 5-0)

Sponsor:	NA
Support:	NA
Oppose:	NA